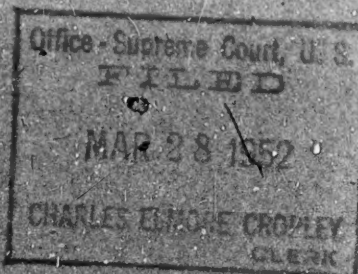


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SUPREME COURT, U.S.



Nos. 428 and 429

In the Supreme Court of the United States

OCTOBER TERM, 1951

PENNSYLVANIA WATER & POWER COMPANY, ET AL.,
PETITIONERS

v.

FEDERAL POWER COMMISSION, ET AL.

PENNSYLVANIA PUBLIC UTILITY COMMISSION,
PETITIONER

v.

FEDERAL POWER COMMISSION

ON WRITS OF HABEAS CORPUS TO THE UNITED STATES COURT
OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL POWER COMMISSION

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No. 428

**PENNSYLVANIA WATER & POWER COMPANY, ET AL.,
PETITIONERS**

v.

FEDERAL POWER COMMISSION, ET AL.

No. 429

**PENNSYLVANIA PUBLIC UTILITY COMMISSION,
PETITIONER**

v.

FEDERAL POWER COMMISSION

**ON WRITS OF CERTIORARI TO THE UNITED STATES COURT
OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT**

BRIEF FOR THE FEDERAL POWER COMMISSION

OPINIONS BELOW

The main opinion of the Federal Power Commission, issued on January 5, 1949, directing a rate reduction (R. XVI, 4845-4997)¹ is reported

¹ The record in these cases consists of eighteen printed volumes and several unprinted volumes of transcripts and ex-

at 8 F. P. C. 1, 82 PUR (NS) 193. Its opinion of February 28, 1949, denying rehearing (R. XVI, 5178-94) is reported at 8 F. P. C. 170, 82 PUR (NS) 286, and its opinion order, issued October 27, 1949, rejecting proposed tariffs and prescribing rate schedules (R. XVII, 5267-5292) is reported at 8 F. P. C. 1193, and its order denying rehearing thereon at 8 F. P. C. 1364. The opinions of the Court of Appeals for the District of Columbia Circuit (R. XVIII, 5367-5393, 5402-5419) are reported at 193 F. 2d 230.²

JURISDICTION

The judgment of the Court of Appeals in these cases was entered on July 3, 1951 (R. XVIII, 5394-5). Petitioners' applications for rehearing,

hibits. We will use roman numerals to refer to volumes and arabic numbers to refer to pages. Taus (Tr. VI, 73) and (R. XVI, 4991) will indicate page 73 in volume six of the unprinted transcript and page 4991 of volume sixteen of the printed record, respectively.

² Additional opinions here relevant are: (1) The opinions of the Court of Appeals for the Fourth Circuit in *Pennsylvania Water & P. Co. v. Consolidated G. E. L. & P. Co. of Baltimore*, 184 F. 2d 552 (C. A. 4), certiorari denied, 340 U. S. 906, 186 F. 2d 934 (C. A. 4) which appear at R. XVIII, 5322-49, 5356-61; (2) the opinion of the Court of Appeals for the Fourth Circuit in *Consolidated G. E. L. & P. Co. of Baltimore v. Pennsylvania Water & P. Co.*, decided January 3, 1952, pending on petitions for writs of certiorari, Nos. 611, 612, this Term. The first decision of the Fourth Circuit will be referred to below as "the first *Consolidated* case," or "the *Penn Water* antitrust case." The second decision will be referred to as "the second *Consolidated* case" or "the *Safe Harbor* antitrust case."

seasonably filed, were denied on September 6, 1951 (R. XVIII, 5399). The petitions for writs of certiorari were filed on November 16, 1951 and granted on February 4, 1952 (R. XVIII, 5419). The jurisdiction of this Court rests upon 28 U. S. C. 1254 (1) and Section 313 (b) of the Federal Power Act.

QUESTIONS PRESENTED

1. Whether the Federal Power Commission's orders reducing rates and prescribing rate schedules for Penn Water are invalidated by the anti-trust laws.

2. Whether the Federal Power Commission orders are invalidated by the laws of Pennsylvania.

3. Whether Penn Water's wholesale sales to its electric utility customers in Pennsylvania are in interstate commerce.

4. Penn Water also presents the question as to whether its status as a "licensee" under Part I of the Federal Power Act exempts it from regulation as a "public utility" under Part II. Since the Commission's orders are based upon and are valid under both Parts, we do not think this question has any materiality in this case.

STATUTE INVOLVED

The pertinent provisions of the Federal Power Act (Title II of the Public Utility Act of 1935, c. 687, 49 Stat. 803, 838, 16 U. S. C. 791a, *et seq.*) appear in the pamphlet copy of the Act submitted with this brief.

STATEMENT

These cases were instituted by the filing under Section 313 (b) of the Federal Power Act of three petitions for review of two orders of the Federal Power Commission in the Court of Appeals for the District of Columbia Circuit. Two of the petitions, one filed jointly by Susquehanna Transmission Company of Maryland³ and Pennsylvania Water and Power Company (Penn Water) on April 22, 1949, and the other filed by the Pennsylvania Public Utility Commission (Pennsylvania Commission) on April 25, sought review of the Power Commission order, issued January 5, 1949, requiring Penn Water to reduce, effective February 1, 1949, its interstate wholesale rates and charges for electric energy by approximately \$2,000,000 and thereby to reduce its net return from about \$3,300,000 to \$1,300,000 annually. The third petition was filed by Penn Water on February 8, 1950, seeking review of the Power Commission's order, issued October 27, 1949, rejecting rate schedules proposed by Penn Water in alleged compliance with the January 5 order and prescribing rate schedules to effectuate

³ Because of doubts as to Penn Water's right to own and operate facilities in Maryland, Susquehanna Transmission Company of Maryland was created as a wholly owned subsidiary of Penn Water to own part of Penn Water's transmission facilities located in that State (R. 1, 20). By virtue of its arrangements with Penn Water, Susquehanna has no separate rates and charges. The references to Penn Water in this brief generally include Susquehanna.

those rate reductions. While these petitions were pending before the court below, petitioners filed motions to annul the Power Commission's orders on the ground that the contract between Penn Water and Consolidated Gas Electric Light and Power Company of Baltimore (Consolidated), on which these orders were allegedly based, had been invalidated as violative of the federal antitrust laws and the laws of Pennsylvania by the Court of Appeals for the Fourth Circuit in Penn Water's private antitrust suit against Consolidated (the first *Consolidated* case).⁴ The court below (one judge dissenting) denied the motions to annul and affirmed the orders of the Power Commission. The facts pertinent to the issues here involved may be summarized as follows:

Penn Water: Penn Water, a corporation organized under the laws of Pennsylvania, owns at Holtwood, Pennsylvania, on the Susquehanna River some nine miles north of the Pennsylvania-Maryland State line, a small steam electric plant and a "run-of-river" hydroelectric project which it operates under a 50-year license issued in 1951 by the Power Commission under Part I of the Federal Power Act (R. XVI, 4847-48, Order of July 3, 1951 in Project 1881).⁵ In addition,

⁴ When the motions were filed, the Fourth Circuit had not yet ruled that the Safe Harbor contract was also invalid.

⁵ The Power Commission ordered Penn Water to apply for a license in 1939 and its order was sustained in 1941. *Pennsylvania Water & P. Co. v. F. P. C.*, 123 F. 2d 155 (C.

Penn Water, in conjunction with Susquehanna, owns and operates transmission lines and associated equipment located in Pennsylvania and Maryland (R. XVI, 4847-48). These transmission lines interconnect with those of Consolidated (the Baltimore electric company) and of Safe Harbor Water Power Corporation (Safe Harbor).⁶ They also interconnect with the facilities of Penn Water's Pennsylvania customers, including the Thorndale-Columbia section of the Pennsylvania Railroad (Railroad), and with the facilities of the Potomac Electric Power Company and of the Perryville (Md.)-Benning (D. C.) section of the Railroad (R. XVI, 4849).

A. D. C.), certiorari denied, 315 U. S. 806. Penn Water thereafter applied for a license, but it did not accept the terms of the tendered license until 1951. In these proceedings, however, Penn Water contended, and the Power Commission agreed, that Penn Water should be treated as a licensee for rate-making purposes (R. XVI, 4864).

⁶ Safe Harbor is a Pennsylvania corporation which owns and operates under a 50-year license issued in 1930 by the Power Commission a large "run-of-river" hydroelectric project on the Susquehanna River several miles above Penn Water's project. All of its stock is owned by Penn Water and Consolidated: 100,000 shares of Class A nonvoting stock are owned by Consolidated and 200,000 shares of Class B voting stock are divided equally between Penn Water and Consolidated (R. XVI, 4850). Safe Harbor's rates and charges have been held subject to regulation by the Commission, both as a "licensee" under Part I of the Federal Power Act, and as a "public utility" under the Act's Part II. *Safe Harbor W. P. Corp.*, 5 F. P. C. 221, 231-243, 66 PUR (NS) 212, 222-223, affirmed, 179 F. 2d 179 (C. A. 3), certiorari denied, 339 U. S. 957.

Penn Water has no franchise service area and does not itself sell to the public. Ever since its incorporation in 1910, Penn Water has disposed of its power in bulk to other utilities. It has never attempted to develop local distribution systems; to enter upon a retail distribution business, to compete with its utility customers for bulk power industrial customers, or to secure substantial monopolized distribution territory (R. I, 32). In addition to its arrangements with Consolidated (see *infra*), Penn Water has contractual obligations to sell firm electric energy to three electric utilities in Pennsylvania,⁷ and to the Railroad for electrified railroad use in Pennsylvania (R. XVI, 4851-54).

The Contract with Consolidated: Under a contract which was entered into in 1931 (R. XV, 4606 *et seq.*) and which was to remain in effect until April 22, 1980 (R. XV, 4607), Penn Water and Consolidated agreed so to operate their power generating facilities that they would obtain "the most effective utilization of output, and coordination in operation, of the two plants" (R. XV, 4606-7).⁸ Under Article II Penn Water

⁷ Metropolitan Edison Company for part of its requirements in York, Pennsylvania; Philadelphia Electric Company for its requirements in Coatesville, Pennsylvania; and Pennsylvania Power and Light Company for its obligations in Lancaster, Pennsylvania (R. XVI, 4853).

⁸ Penn Water and Consolidated were also party to a fifty-year agreement, effective June 1, 1931, with Safe Harbor, the third member of the power pool. Under the Safe Harbor

agreed to deliver to Consolidated all of Penn Water's capacity and energy "not otherwise disposed of in performance of now existing contracts, new contracts entered into by [Penn Water] with Consolidated's approval or any duty or obligation to serve imposed on [Penn Water] by its charter or otherwise by law" (R. XV, 4607-4608; XVI 4851). Penn Water, in turn, was entitled to obtain from Consolidated steam-generated energy in excess of Consolidated's own requirements up to the limits of the latter's available generating capacity to enable Penn Water to meet its firm power obligations in Pennsylvania (R. XV, 4585; XVI, 4851).⁹

contract, Safe Harbor agreed with Consolidated and Penn Water (and the latter *inter sese*), that in return for a combined annual payment which would yield to Safe Harbor a specified rate of return after operating expenses (including taxes and depreciation) the latter companies should be entitled to *all* of the capacity and energy available from Safe Harbor's project in the ratio of two-thirds to Consolidated and one-third to Penn Water (R. XV, 4554-4576; XVI, 4851). Although under the arrangements the payment obligation is prorated between Penn Water and Consolidated in the ratio of their capacity and energy entitlements, the power generated by Safe Harbor is at the disposal of the power pool to permit the maximum utilization of the resources at lowest cost (R. I, 26; V, 2137-2138; XIII, 4369). This is the contract which, because of other provisions, the Fourth Circuit held to be invalid under the antitrust laws in the *Safe Harbor* antitrust case, in which petitions for certiorari are now pending in Nos. 611, 612, this Term.

⁹ Consolidated's generating facilities, the principal steam-electric resources of the pool, consist now of four steam-electric plants of 385,000 kw. capacity. Safe Harbor's gener-

For the residue which it received from Penn Water, Consolidated paid in accordance with a formula contained in Article III whatever dollar amount was necessary, in addition to Penn Water's revenue from its customers, to cover all of Penn Water's cost of operation (including taxes and depreciation) and to provide Penn Water with a formula-determined rate of return on investment (R. XV, 4608-12; XVI, 4851) which amounted to from 9.9% to 12.4% per year between 1931 and 1945 on the rate base used by the Commission (R. IX, 3593). The formula for the computation of the amount Consolidated paid to Penn Water included credits to Consolidated for its deliveries to Penn Water and for Penn Water's diversion to its own use, with Consolidated's consent, of energy purchased by Consolidated under the contracts.

Article VIII provided for the appointment by each party of "one representative to act as its agent for investigation, consultation, and advice in all operating, engineering and accounting matters pertaining to the interconnected facilities herein contemplated, and to the supply and interchange of power and exchange herein provided for. * * *

These representatives to be known as the Operating facilities are exclusively hydro, its plant having an effective capacity of 230,000 kw. Penn Water's generating facilities are principally hydro with an effective capacity of 104,000 kw.; its steam-electric plant has a capacity of only 20,000 kw. (R. XVI, 4848, 4974).

ing Committee shall confer upon request of either; in case of their inability to agree, the question in dispute shall be submitted to the Presidents of the respective companies for their decision" (R. XV, 4614). The purpose of these arrangements, as stated in Article VIII, was "to encourage the maximum utilization of the power and energy entitlements and resources and other facilities of the parties * * * to the end that the joint use of this property and equipment shall give the greatest practical benefit to the public" (R. XV, 4613-4614; XVI, 4859-4860).¹⁰

In addition, Article IV of the contract required Penn Water to "obtain the approval of [Consolidated] before entering into any agreement or agreements * * * for the sale and/or purchase and/or interchange of electrical and hydraulic power and energy, or before making any substantial modification in the existing contracts now in force between [Penn Water] and its customers other than [Consolidated]" (R. XV, 4612). Article V similarly required the obtaining of Consolidated's approval before Penn Water incurred "any single commitment for investment (except for renewals or replacements) in excess of \$50,000 on the basis of which [Con-

¹⁰ Article VIII goes on to provide that the parties " * * * shall so conduct their operations that economic interchange of power and energy during the different hours of the day, the seasons of the year, and over more prolonged periods, shall be encouraged in every possible way" (R. XV, 4614; XVI, 4860).

solidated] shall make payment" under the payment provision (R. XV, 4612-3).

The Power Pool: As a result of the arrangements as to power pooling and residual method of payment, Penn Water has been able to operate in a manner not otherwise possible because of the unusual nature of its system. Since its hydro plant, which constitutes the bulk of its energy resources, is essentially, a "run-of-river" plant,¹¹ Penn Water's ability to provide dependable capacity from its own resources is limited by the amount of water available in the Susquehanna¹² River, which "is one of the most variable flowstreams of large size in the country" (Tr. III, 1236).¹² Most of the time there is not enough river flow to permit the operation of Penn Water's hydro plant to the full electric capacity of the generators.¹³ At times of low flow it does not have sufficient capacity to supply the demands of its customers. Consequently, if dependent solely upon its own generating facilities to supply the firm power loads of its customers, it could not do so (R. V, 2149; Tr. X, 3626). For the

¹¹ Penn Water's hydraulic storage capacity is sufficient only to provide for a weekly cycle of drawdown and refill (R. I, 438-439).

¹² The flow of the river fluctuates widely from a low of 2,100 cubic feet per second to a high of 860,000 c. f. s. (R. I, 39).

¹³ The Penn Water hydro plant can utilize a maximum of 31,500 c. f. s. (Tr. LIX, 22536), with the river flow more often than not being substantially less (Tr. LVIII, 22371; LXVI, 24764).

periods of low and high flow of the river do not coincide with periodic low and high demands for electric energy, which characteristically occur in daily, weekly and yearly cycles, each with its own peak;¹⁴ since electric energy cannot feasibly be stored, all demands must be satisfied by capacity sufficient to produce electric energy instantaneously as customers switch on their lights, motors, and other appliances.

Moreover, if operated independently, Penn Water could not have made the most effective utilization of the potential resources of the river nor could it have obtained the maximum economy of generation (R. I, 25, 74-75, 440-441). Penn Water's inability to impound water during high-flow months for use in subsequent low-flow months, and the frequent recurrence of low river flows, limits its dependable capacity (R. I, 41, 2212-2216; XVI, 4971-72). These physical limitations, plus the excessive capital investment required for producing the relatively small dependable output,¹⁵ would preclude Penn Water, if

¹⁴ Daily peaks are usually in midmorning or midafternoon when industrial activity is highest, or in the early evening hours when residential use overlaps commercial and industrial uses. Weekly peaks usually occur in the first five working days of the week; weekly lows on week ends (and holidays). Yearly peaks usually occur in winter when darkness falls before the close of the working day, and frequently during the pre-Christmas period, when unusually high commercial and residential uses coincide with high industrial use (R. I, 42; Tr. LXV, 24222).

¹⁵ Since the continuous output of the Penn Water plant at

operated independently, from competing successfully with steam plants and substantial water would have to be wasted over the spillways at times of high flow (R. I, 25; Tr. III, 1236).

Under the power pool arrangements worked out by Penn Water and Consolidated, Penn Water's hydro facilities have been integrated into a system which has steam generating facilities and supplies a large utility load (R. I, 32-33, 439; R. XVI, 4849-4850, 4857, 4987); this results in the most effective and economic use of Penn Water's hydro resources. Penn Water has been able to take on firm obligations and to meet them through the availability of power from Consolidated's steam-generation plants (R. V, 2397), which normally are capable of producing up to their full capacity;¹⁶ in times of severe water shortage, Consolidated carries the main burden of

low water (2,100 c. f. s.) is only about 8,500 kw., the investment per kw. would be \$3,897, compared to an average investment of \$316 per kw. for electric plant in service of companies whose electric operating revenues are more than \$250,000 per year. R. XVI, 4992; Tr. III, 1236; *Statistics of Electric Utilities in the United States* (Federal Power Commission 1950), p. xxi.

¹⁶ Steam plants, not shut down for emergency or for scheduled maintenance, are usually capable of producing up to their full capacity at all times, including peak-load periods (R. VI, 2455), and usually are used in the order of their efficiency—the newer, larger, more efficient units being used most continuously (base-load operations), the less efficient units being put into operation for shorter periods as the load increases (peak-load operation) (R. I, 23, 36-37; VI, 2455).

supplying Penn Water's customers (R. XIV, 4405; XVI, 4981).

In addition, during periods of low river flow, Penn Water's hydro plant is shut down during daily and weekly off-peak load hours to permit water to accumulate. The steam plants of the pool are utilized to carry the load during such periods. Then during peak-load hours, the hydro plant is operated at full capacity for a few hours using the water which has accumulated during the period of non-use (R. I, 37, 439; VI, 2455; XVI, 4988; Tr. LIII, 20137). Through such peaking operation, Penn Water's hydro plant is used to the best advantage by contributing its maximum generating capacity to the system during peak-load hours when maximum capacity is needed and by saving the costs of using the oldest and most inefficient steam plants which would otherwise be used (R. I, 38-42; VI, 2455; XVI, 4988).¹⁷ On the other hand, when the river flow is high, the hydro plant is operated around the clock to carry the base load of the pool in substitution for steam-generated energy, thereby reducing the amount of fuel which would otherwise

¹⁷ The availability of the hydro energy avoids the installation of additional steam capacity and the necessity of keeping existing boilers banked and ready for use (R. I, 24, 38); which would involve standby losses and the operation of turbo-generators below their most efficient loading. The hydro capacity is also instantly available, coming from standstill to full loads in a fraction of a minute (R. I, 42; XVI, 4849-4850).

have to be burned and minimizing the waste of water (R. I, 36-37, 40, 75; VI, 2455; Tr. III, 1236, 1246-1247; XVI, 4988). As a result, the flow of energy is generally south from Pennsylvania toward Maryland at all times during the spring months when the river is high (R. I, 341; XVI, 4860). During the rest of the year, the practice is to generate energy at Penn Water's hydro plants so as to assist Consolidated in carrying its peak loads during the day, but to stop hydro generation so as to allow the ponds to refill during off-peak periods (R. I, 45-46, 439; R. XVI, 4860). And, although at such times the flow of energy tends to be to the north, from Baltimore to Pennsylvania, the direction of flow on the lines crossing the State boundary may change frequently according to the needs of the consumers in Pennsylvania or Maryland (R. I, 341; II, 599-600; VI, 2455; XVI, 4860; Tr. LXVI, 24733).

The Residual Method of Payment.—The residual method of payment provided in the contract (*supra*, p. 9) is an essential element to the successful operation of the power pool, the purpose of which is to have energy provided by the source which is most economical at the particular time, regardless of whether owned by Consolidated or Penn Water. Rates based on units of service would, of course, have impelled each party to operate so as to derive the maximum advantage for itself under such rates. This would not bring about the maximum utilization of the power re-

sources of the Susquehanna and the lowest possible joint costs of production, for it had proved impossible to devise unit rates adequate to that purpose, as Penn Water's officials testified.

John A. Walls, then president of Penn Water, testified before the Commission that the unit basis rate which was used in the 1927 contract between the parties "militated against the correct principles of operating a combined hydro-steam generating and supply system" (R. I, 26), and that it was not until the method of payment was changed to "an annually computed lump sum, independent of the number of kilowatts and kilowatt hours, that * * * the most economical result obtainable from the combined power resources could be derived" (*ibid.*).

George W. Spaulding, then vice president and now president of Penn Water, similarly testified that maximum coordinated use of combined resources was not achieved under the unit basis rate used prior to the 1931 agreement with Consolidated, since the customers "were inclined to view their own power requirements as matters distinct from the requirements of other customers" (R. I, 72). Mr. Spaulding described some of the methods of payment which had been tried but had not worked out satisfactorily (R. I, 71):

The evolution of Penn Water's power agreements with its customers in Baltimore

included the early extreme of a stipulated capacity service always available and price on a kilowatt-year basis, combined with additional energy sales at a stated mill rate during specified hours of the day.

Another form of sale was a stipulated capacity service combined with a limited amount of yearly energy at a stated mill rate to be taken at the customer's desires.

Neither form of contractual arrangement recognized the possibility of energy purchases in large volume during the periods of ample flow, nor the coordinated scheduling of the available steam resources in the interest of operating economy.

See also n. 34, p. 47, *infra*.

The residual method of payment provided in the 1931 contract, on the other hand, Mr. Spaulding went on to state, had the advantages of removing "all artificial barriers which would interfere with the hour-to-hour, day-to-day and the long range coordination of the power resources of the companies involved. Such a goal had not been as fully achieved by Penn Water and [Consolidated] in two decades of preceding power relations" (R: I, 71). As a result, under that form of payment (R. I, 75).

[a]ll of the objectives desired in 1931 have been attained. The Safe Harbor project was successfully constructed, financed and brought to a proper earning

level. The most effective utilization of the system steam capacity and energy and that of our hydro plants has been fully achieved, with the resulting conservation of fuel, particularly during the critical days of fuel shortage in the recent national emergency, of benefit to the public.

The ability to supply the Pennsylvania Railroad Company at several widely separated points, to the convenience and advantage of the customer, would not have been possible had it been sought separately by Penn Water or by Baltimore Company, operating under a contractual arrangement that was complicated with artificial barriers.

In brief, therefore, the effect of the residual payment was to eliminate the conflict of interests between Penn Water and Consolidated as to the use to which Penn Water's facilities should be put, and to make Penn Water's facilities fully available for pool purposes, with both Penn Water and Consolidated motivated by the common interest of deriving the maximum benefit from these facilities as part of the pool (R. XVI, 4860). As stated in its 1941 Report to Stockholders, the pooling of resources (of which the method of payment was an essential part) solved for Penn Water the problem

of providing, without large and expensive reservoirs, a uniform supply of power while utilizing the unharnessed energy of a drainage area subject to severe droughts

and floods. The average daily flow at Holtwood has varied from as little as 1,700 cubic feet per second up to 756,000 cubic feet per second since the Company began operations. Nevertheless out of this difficult situation, an important and reliable power pool has been developed.

The answer to the problem was combined hydro and steam supply; not the substitution of hydro for steam, but from the outset the integration and coordination of hydro and steam in the planning for the capacity needed and in the operation and maintenance of the facilities [R. XVI, 5183].

The residual method of payment thus enables Penn Water's hydro facilities to be integrated with the generating facilities of Consolidated as well as Safe Harbor. It permits the energy used to satisfy demands of customers of either to be determined on the basis of maximum utilization and economy (*i. e.*, river flow, relative costs of steam generation, and magnitude of loads) (R. I, 40; II, 599-600; XVI, 4987).

The Power Commission's order of January 5, 1949: On September 1, 1944, having received petitions from the Mayor and City Council of Baltimore, Maryland and from the Public Service Commission of Maryland (Maryland Commission) (R. XV, 4623, 4731-4733),¹⁸ the Power

¹⁸ The importance of the interstate rates to Consolidated's retail rates to consumers, which were at the time the subject of a Maryland Commission rate proceeding, is referred to

Commission instituted an investigation into the reasonableness of the rates and charges made by Penn Water for its interstate sales of electrical energy at wholesale, including its sales to Consolidated (R. XVI, 4837).¹⁹ After extensive hearings, in which the Maryland and Pennsylvania Commissions actively participated as intervenors on opposite sides (R. I, 2; XVI, 4837-4843), the Power Commission on January 5, 1949, issued its opinion and order (R. XVI, 4845-4997a).

After reviewing the operations of the power pool, the Commission found that since all of the resources of the pool are available to meet the combined load of its members, without reference

by that Commission in its opinions in its investigation. *Re Consolidated Gas Electric Light and Power Company of Baltimore*, 61 PUR (NS) 94, 102-103; *id.*, 67 PUR (NS) 144, 149-150.

¹⁹ The Power Commission simultaneously and on the same petitions initiated a separate investigation of the rates charged by Safe Harbor to Consolidated. On November 4, 1946, after extensive hearings, the Commission, no question as to the antitrust laws having been raised, directed the continuance of the entire Safe Harbor contract with the exception of the rates which it ordered reduced by about \$627,551 annually. The Commission there construed the contract as providing that Safe Harbor's total output (not the residual left after certain contracts were met, as suggested by Penn Water (Br. No. 428, p. 8 n.)), was to be divided between Penn Water and Consolidated on a $\frac{1}{3}$ - $\frac{2}{3}$ basis. *Safe Harbor W. P. Corp.*, 5 F. P. C. 221. Upon review, the Court of Appeals for the Third Circuit affirmed the order. *Safe Harbor W. P. Corp. v. Federal Power Commission*, 179 F. 2d 179 (C. A. 3), certiorari denied, 339 U. S. 957.

to state boundaries, the pool was an "integrated and coordinated interstate electric system" (R. XVI, 4857). The Commission further found that the wholesale sales of system energy, such as those by Penn Water to its Pennsylvania utility customers, made without reference to the state of origin of the energy, were pool sales, and hence, in light of the interstate nature of the pool, were sales for resale in interstate commerce (R. XVI, 4861). The Commission accordingly concluded that Penn Water is a "public utility" under Part II of the Federal Power Act by virtue of its ownership and operation of facilities for the transmission and sale at wholesale of electric energy in interstate commerce, and that its sales for resale to Consolidated and to its three Pennsylvania customers are subject to Commission jurisdiction under Section 206 (a) of the Act (R. XVI, 4862).²⁰

In addition, the Commission found that it had jurisdiction to regulate Penn Water under Section 20 of Part I, which relates *inter alia* to the rates of licensees whose power enters interstate commerce, since, as it found, the States were "unable to agree" on these rates (R. XVI, 4864). The Commission further found that Penn Water's status as a "licensee" under Part I does not exempt it from regulation as a "public utility" under Part II and that no conflict resulted in the

²⁰ The Commission did not assert jurisdiction over Penn Water's sales to the Railroad (R. XVI, 4857, fn. 18).

pending case from regulation under both Parts (R. XVI, 4865).

In determining just and reasonable rates, the Power Commission found Penn Water entitled to a return of \$1,300,672, computed on a "fair and reasonable rate of return" of $5\frac{1}{4}\%$ ²¹ on a proper rate base of \$24,774,712²² (R. XVI, 4992). The Commission fixed the return at $5\frac{1}{4}\%$ since (1) under the arrangements with Consolidated which the Commission directed be continued as "the most practicable under the circumstances" (R. XVI, 4981), Penn Water was assured a stabilized income as in the past (R. XVI, 4953), and (2) cost of capital studies showed that such a return, based on Penn Water's actual cost of 3.17% for bond money and 5.21% for preferred stock, allowed about 8.64% for equity capital, which the Commission found to be adequate (R. XVI, 4954-57).

Since Penn Water's net operating income exceeded a fair return by \$1,954,261, the Commission undertook to determine "a reasonable and

²¹ Penn Water's statement (pp. 17, 52) that the Commission by subsequent order reduced the rate of return to $4\frac{3}{4}\%$ has no foundation. The item of \$141,777 upon which this argument was based in the court below was taken into account in the Commission's original opinion reducing rates. (R. XVI, 4961, 4980-4981, 4993-4994). In any event, the contention was not accepted by the court below and has not been brought here for review.

²² This rate base consists of gross investment of \$33,126,585 plus working capital of \$650,000 less accrued depreciation of \$9,001,873 (R. XVI, 4992).

proper allocation, of the cost of service rendered by Penn Water" (R. XVI, 4981, 4992). On the basis of that allocation, which the Commission grounded on the representative costs of Penn Water's services, which it directed to be continued, to its Pennsylvania utility customers and to Consolidated, the Commission ordered Penn Water to lower its rates in a manner which, on the basis of 1946 operations, would result in a reduction to its Pennsylvania utility customers by the aggregate sum of \$220,943 and to Consolidated of \$1,733,318²³ in Consolidated's residual payments (R. XVI, 4980-81, 4993, 4995-96).²⁴ The Commission, accordingly, directed Penn

²³ While the revenue Penn Water received directly from Consolidated exceeded a reasonable return by about \$700,000, the Commission directed that Consolidated receive a credit for the revenues received by Penn Water from its Pennsylvania utility customers for economy interchange energy belonging to Consolidated. This credit of \$1,127,699 and other adjustments resulted in increasing Penn Water's excess revenues from Consolidated to \$1,733,318. See *infra*, pp. 81-83.

²⁴ The Commission prescribed formula differed from that provided for in the contract in the following particulars, among others: The rate of return was reduced to 5¼%; the rate base to which the 5¼% was to be applied was changed from an undepreciated rate base to a rate base computed by deducting accrued depreciation from gross investment and including working capital; the method of computing the annual allowance for depreciation was changed from a sinking-fund depreciation method to the straight line method, thereby increasing the annual allowance (R. XVI, 4992-93; R. XVII, 5279-5283; Tr. III, 1136-8, 1159-60; R. XV, 4608-12, 4617-21).

Water to file a "new schedule of rates and charges for ~~(or) and~~ in connection with its transmission and sale of electric energy in interstate commerce for resale" to its Pennsylvania utility customers and Consolidated to effectuate the prescribed reductions as of February 1, 1949, reserving the right to reject the schedules and in lieu thereof to prescribe appropriate schedules by its own further order (R. XVI, 4995).

Petitioners sought rehearing of this rate reduction order of January 5, 1949. In its petition for rehearing Penn Water urged for the first time that the 1931 agreement, and particularly Articles IV and V thereof (see *supra*, p. 10), violated the Federal antitrust laws and the laws of Pennsylvania (R. XVI, 5012), and consequently that the Commission's findings as to jurisdiction, rate of return and allocation, were invalid (R. XVI, 5012, 5014, 5042, 5054, 5055, 5136-37, 5138). In so urging, Penn Water referred to its complaint filed in December 1948 against Consolidated in the United States District Court for the District of Maryland in which it sought a declaratory judgment that the Consolidated contract was invalid under the antitrust laws and the laws of Pennsylvania (R. XVI, 5013). The Power Commission denied the petitions for rehearing (R. XVI, 5178-5194) with the comment (R. XVI, 5184).

If there are questions as to the legality of the foundation contracts which are in liti-

gation, as [petitioners'] application for rehearing indicates, the validity of our order is not dependent upon the decision of those questions. In our opinion and order we took care to leave the continuation of the operation of the integrated and interconnected system in full effect, merely changing the rates, * * * .

Following the denial of their second petitions for rehearing, Penn Water, on April 22, 1949, and the Pennsylvania Commission, on April 25, petitioned the court below for review of the Power Commission's January 5 order.²⁵

The Power Commission's order of October 27, 1949: Thereafter, on May 31, 1949 Penn Water filed with the Commission rate schedules purportedly in compliance with the January 5 order (R. XVII, 5248-5266). On October 27, the Power Commission rejected these schedules after finding that they did not comply with the January 5 order in several respects. The Commission prescribed its own schedules which it found would effectuate the requirements of its order

²⁵ By order dated April 29, 1949, the court below had stayed the January 5 order of the Commission insofar as it provided that the new rate schedules should be effective February 1, 1949, but had refused to suspend the requirement that rate schedules be filed and the Commission's reservation of the right to reject the schedules and in lieu thereof to prescribe appropriate schedules by its own further order. The court stayed the effective date of the required schedules on the condition that Penn Water segregate the amount of the prescribed rate reduction in a special reserve.

and would allow Penn Water the 5 $\frac{1}{4}$ % return prescribed (R. XVII, 5277-5278). The Schedule pertaining to Consolidated, after detailing the means by which the new rate was to be determined (R. XVII, 5279-5283), contains the following final paragraph, which is of significance in this case:

The foregoing provisions supersede only the *rates and charges heretofore made, demanded, collected or assessed against Baltimore Company by Penn Water and Transmission Company. All other provisions of the aforementioned contracts, in and of themselves lawful prescribing or defining the power, energy and transmission services to be furnished; or any classification, practice, regulation or rule affecting such services*, which several provisions are incorporated herein by reference, shall be observed and be in force. [Italics supplied.]

After denial of its application for rehearing of this order, Penn Water filed in the court below an additional petition seeking review of this order (R. XVII, 5222-5231).

The proceedings below: While these cases were pending in the court below and after briefs on the merits had been filed by all parties, petitioners moved the court to annul the Power Commission's orders on the ground that they had been deprived of essential factual and legal support by the decision rendered by the Court of Appeals for the Fourth Circuit in Penn Water's first private

antitrust action against Consolidated (R. XVIII, 5322-49).²⁶ The court below, however, denied the motions to annul. It construed the Fourth Circuit decision—

as having done no more than declare illegal under the antitrust laws certain restraints exercised by [Consolidated] upon Penn Water—such as requiring its approval before it could take on new customers or expand generating facilities. Those restraints had been privately agreed upon by the parties and submitted to the Commission as an accomplished fact. The court was careful to avoid using language which might be interpreted in such fashion as to affect any rate proceeding * * * [R. XVIII, 5374-75].

Accordingly, the court stated (R. XVIII, 5375):

In our view, the Fourth Circuit's opinion neither purported to nor did relieve Penn Water from its obligation under the Federal Power Act to continue the then-existing services and rates. It is those services and rates, reflecting underlying operations, which were the subject of the Commission's order. "A rate is not necessarily illegal because it is the result of a conspiracy in

²⁶ The Fourth Circuit's decision reversed the ruling of the District Court for the District of Maryland holding that the contract was valid and dismissing Penn Water's complaint. *Pennsylvania Water & P. Co. v. Consolidated G. E. L. & P. Co. of Baltimore*, 89 F. Supp. 452.

restraint of trade in violation of the Anti-Trust Act. What rates are legal is determined by" the regulatory statute [citing *Keogh v. Chicago & N. W. Ry. Co.*; 260 U. S. 156, 162]. The validity of Commission action in this proceeding must be determined in light of the criteria furnished by the Federal Power Act, as applied to the operations and arrangements under scrutiny.

As to petitioners' attacks on the jurisdictional basis of the Commission's orders, the court held that Penn Water was part of an "integrated and coordinated interstate electric system," that its sales to its Pennsylvania utility customers were in interstate commerce, and that, consequently since these sales are for resale, Penn Water was a "public utility" under Part II of the Federal Power Act, with the rates for those sales subject to regulation under that Part (R. XVIII, 5382-85). The court also ruled *inter alia* that the fact that Penn Water is a licensee under Part I, does not prevent it from also being regulated as a public utility under Part II (R. XVIII, 5378-81), and further that since there was substantial evidence to support the finding that the Maryland and Pennsylvania Commissions were "unable to agree," the Commission was also authorized to regulate Penn Water's wholesale interstate rates as a licensee under Section 20 of Part I (R. XVIII, 5381-82).

On the merits, the court ruled that the Power Commission's findings were supported by substantial evidence (R. XVIII, 5385-5393) and, accordingly, it affirmed (R. XVIII, 5393).

SUMMARY OF ARGUMENT

I

The Power Commission's order was a valid exercise of its power to prescribe just and reasonable rates. An important stated purpose of the Power Act was to procure the most efficient use of the nation's power resources. It was proper for the Commission to take this factor into account in prescribing a rate schedule based upon the continued integration of the hydro facilities of Penn Water with Consolidated's steam plants. This consideration fully justifies the use of the residual payment formula, in order to assure the most economic use of the combined resources of the two companies. Indeed, petitioners no longer seem to question that the Commission's order conforms to the standards of the Power Act.

II

A. 1. The Commission's order prescribing the rate schedule is not subject to the antitrust laws. Although an express statutory exemption may be necessary to permit an administrative agency to authorize private conduct which would otherwise violate the antitrust laws, here we are concerned with a governmental order binding of its

own force. Such governmental action and conduct taken pursuant thereto to avoid statutory penalties has never been deemed subject to the antitrust laws. For the Sherman Act only applies to private combinations and monopolies, not to the acts of governmental agencies within the scope of their authority. *Parker v. Brown*, 317 U. S. 341.

2. Furthermore, in this case we are dealing with a rate order. Such statutes as the Federal Power Act govern industries in which the processes of competition cannot be counted on adequately to protect the public. It has long been recognized that rates are to be regulated in accordance with the standards of the controlling statute. An agency administering such a statute may weigh many factors in addition to antitrust criteria, and is not precluded from prescribing arrangements which might be unlawful under the Sherman Act if contained only in private agreements. As long as a rate order is authorized by the pertinent regulatory statute, the Sherman Act is inapplicable. This principle is sufficient to dispose of this case, since the Power Commission has authority, in fixing rates, to include provisions prescribing both the service to be rendered in return for the rate fixed and the formula by which the rate is to be computed. The provisions prescribing the residual method of disposing of Penn Water's power to Consolidated and of determining the amount

Consolidated was to pay were thus entirely appropriate in the rate order. The remaining provisions of the order, including those provisions incorporated by reference from the contract, were merely ancillary to these provisions.

B. The foregoing considerations also make it plain that the Commission's order does not violate the antitrust provision of the Power Act, Sec. 16 (h). That section, like the Sherman Act, does not apply to governmental action in the field of rate regulation.

C. The Commission has not ordered the continuance of any contractual provision held unlawful by the Fourth Circuit or otherwise in violation of the antitrust laws. In the first *Consolidated* antitrust case, the Fourth Circuit held only that Articles IV and V of the Penn Water-Consolidated agreement violated the antitrust laws. It did not suggest that the power-pooling and residual method of payment were unlawful, but the contrary. The Power Commission, on the other hand, only prescribed as a part of its order portions of the contract "in and of themselves lawful," a reservation properly construed as excluding the specific provisions which the Fourth Circuit held to be unlawful. The Fourth Circuit and the court below both agree on this.

D. Petitioners' argument that the Commission's order must fall because based upon continuance of the private contract which the Fourth Circuit

held invalid ignores the fact that the order supplants the contract and stands on its own feet. The fact that the order in general follows the plan of the contract, though with important changes in the basic provisions governing rates, and adopts by reference certain of the contract's provisions, does not mean that the order continues the contract *qua* contract.

In any event, since the antitrust laws do not apply to the Commission's order, it is immaterial whether any provisions of the order might violate the antitrust laws if viewed as private contractual arrangements.

II

The Commission's order is not invalid because in conflict with the laws of Pennsylvania. The only provisions held by the Fourth Circuit to violate the Pennsylvania laws were Articles IV and V, and they were not prescribed by the Commission. Furthermore, analysis of the Pennsylvania laws referred to, which are merely the general utility and corporation laws which preclude a corporate management from abdicating its functions, indicates that they would not bar a reasonable business arrangement necessary to permit efficient operation of the corporation's resources. No Pennsylvania authority holds otherwise. In any event, if the Commission's action is authorized by the Power Act, Pennsylvania law cannot stand in the way. The fact that Con-

gress was not seeking to regulate rates formerly subject to state control does not mean that the federal regulation of interstate wholesale rates was to be restricted by state law. *Public Utilities Commission v. United Fuel Gas Co.*, 317 U. S. 456, 466-467; *Illinois Natural Gas Company v. Central Illinois Public Service Company*, 314 U. S. 498.

IV

Petitioners assert that the Commission's order is based upon provisions of the Safe Harbor contract held unlawful by the Fourth Circuit in the second antitrust case. But the Commission relied upon its own order prescribing the contract (as modified so as to reduce the rates) as the rate schedule in that case, not upon the contract as such. That order, sustained by the Third Circuit (*Safe Harbor W. P. Co. v. Federal Power Commission*, 179 F. 2d 179, certiorari denied, 339 U. S. 957) cannot be attacked in any other court collaterally in a private suit to which the Commission is not a party. The doctrine of primary jurisdiction clearly requires resort to the Commission initially in any proceeding to invalidate or modify its order. Furthermore, the Safe Harbor rate order, as governmental action in the field of rates, cannot violate the antitrust laws. See Point II A *supra*. The Fourth Circuit's decision in the *Safe Harbor* case disregards these fundamental principles and was clearly erroneous.

V

Penn. Water's sales to its Pennsylvania customers were sales in interstate commerce, as both the court below and the Third Circuit in the *Safe Harbor* cases have held. The Pennsylvania customers received power which, depending on the flow of the Susquehanna, came from Penn. Water's plant in Pennsylvania or Consolidated's plants in Maryland. Interstate and intrastate energy, often commingled, could not have been purchased as a source of firm power except as a unit. The entire sale is thus properly treated as interstate. Interstate commerce is a practical conception. Obviously, the sale of the energy of an integrated system cannot be divided into interstate and intrastate segments so as to enable a State commission to regulate the energy sold in a period of high-water flow and the federal commission in other periods when the power moves interstate. The rates for such an inseparable transaction must be controlled by the single agency which can have jurisdiction over all of them—which means the federal commission.

VI.

The contention that a licensee subject to regulation under Part I of the Power Act may not also be regulated under Part II, is irrelevant here since Penn. Water's rates were lawfully fixed under both Parts. In any event, the language

as well as express and authoritative statements in the legislative history demonstrate that companies which were both licensees under Part I and public utilities under Part II were to be subject to regulation under both. The Parts do not impose inconsistent regulations; indeed, in so far as rates are concerned, the statutory language is substantially identical.

ARGUMENT

INTRODUCTORY

The Commission's investigation into the reasonableness of Penn Water's rates for wholesale sales in interstate commerce was instituted on September 1, 1944. As a result of extensive hearings held for over a year, in which a record of 21,279 pages of testimony and of 605 exhibits was compiled, the Commission found in 1949 that Penn Water's net return was about two and a half times what it should be and ordered a rate reduction of approximately \$2,000,000 a year,²⁷ to be allocated among Penn Water's wholesale customers in accordance with the arrangements which it prescribed. In reaching this conclusion, the Commission found that the plan for the pooling of power resources previously agreed to by Penn Water and Consolidated in 1931, including the residual method of payment, was the "most

²⁷ The Commission found Penn Water entitled to a return of \$1,300,672 (*supra*, p. 22).

practicable" means of overcoming the problems presented by the extremely variable flow of the Susquehanna River, and of achieving the maximum utilization and economies from their combined hydro and steam generating facilities. The Commission, accordingly, directed that these arrangements should be continued in the public interest.

As the cases come before this Court, petitioners no longer attack the merits of the Commission's rate reduction; they do not claim that the orders are not supported by substantial evidence or that the rate reduction was excessive.²⁸ Their primary argument—apart from the Pennsylvania's Commission's challenge to the finding of interstate commerce—is that in private litigation the 1931 contract had been held to violate the antitrust laws and that the Commission's order reducing rates was based upon this contract and therefore must fall. Thus, petitioners are invoking the anti-trust laws to frustrate the public interest in an already long delayed rate reduction, the propriety of which in and of itself is no longer challenged.

The Government—which in this case includes both the Federal Power Commission and the De-

²⁸ Nor do they attack the allocation of the rate reduction except collaterally, in support of the contention that the Commission relied on the allegedly illegal contracts in determining how the allocation should be made. Brief in No. 428, pp. 55-58; Brief in No. 429, pp. 32-42. Neither petition for certiorari raised a question as to the validity of the allocations as such.

partment of Justice (which is charged with primary responsibility for enforcing the antitrust laws)—does not regard these cases as presenting any clash between antitrust enforcement and a regulatory agency. For the Power Commission has not ordered the continuance of any contractual provision held unlawful by the Fourth Circuit or otherwise in violation of the antitrust laws. And the Fourth Circuit, which has held that the Commission is without power to prescribe conduct otherwise illegal, agrees that the Commission has not undertaken to do so in this case.

The Commission's order prescribing the entire contract in the *Safe Harbor* case, which was upheld by the Third Circuit²⁹—but which is nevertheless attacked by petitioners in this case on the ground that the order here involved is based in part on the *Safe Harbor* contract—does not represent any different attitude or approach. No antitrust objection was raised before the Commission or the court in that case. What the Commission would do if the problem were presented to it in connection with the *Safe Harbor* order cannot be foretold. But certainly the Commission itself, not the District Court in Maryland, is the proper forum for either a new challenge to the validity of its order or an attempt to have the order narrowed or otherwise modified.

²⁹ *Safe Harbor W. P. Corp. v. Federal Power Commission*, 179 F. 2d 179, certiorari denied, 339 U. S. 957.

For the above reasons we think it plain that the Commission has in no way sought to curtail the scope of operation of the antitrust laws with respect to the contracts involved in these cases. It is true that the Commission did prescribe the rates in accordance with a formula which, though not claimed to be unauthorized under the Federal Power Act, petitioners assert to be in violation of the antitrust laws and laws of Pennsylvania. But a long line of cases establishes that the Interstate Commerce Commission and those agencies, including the Federal Power Commission, whose statutes are modeled in large part on the Interstate Commerce Act, are supreme when it comes to rates, and that rates which comply with the standards of the regulatory statutes are lawful and must be observed even though the utilities involved may be subject to the antitrust laws for acting in combination in fixing the rates or in other respects. See particularly *Georgia v. Pennsylvania Railroad*, 324 U. S. 439. Here all that the Commission has prescribed is a rate schedule. The residual payment plan is the method by which the rates are to be computed, not an independent restrictive contractual provision. Indeed, the Commission's final order of October 27, 1949 fully defines the method of payment (R. XVII, 5279-5283) and thus completely supplants the Article of the contract dealing with that subject.

Clearly, this rate provision contained in the Federal Power Commission's order, superseding that in the private contract, is valid if authorized by the Federal Power Act. Petitioners' briefs do not seem to challenge the validity of the Commission's order in that aspect. Nevertheless, since the authority of the Commission to prescribe the order which it actually entered is vital to almost every feature of this case, we shall show in Point I (*infra*, pp. 39-48), that the Federal Power Act clearly authorizes the Commission to enter the order here involved. We shall then show, in Point II (*infra*, pp. 49-84), in more detail than we have in this introduction, that this case presents no problem as to possible conflict between the Power Commission order and the Sherman Act, and that if it did, the Sherman Act does not apply to conduct prescribed by the Federal Power Commission.

I

THE POWER COMMISSION'S ORDER WAS AUTHORIZED BY THE FEDERAL POWER ACT

The provisions of the Federal Power Act applicable to Penn Water as both a "public utility" and a "licensee" (see *infra*, pp. 117-137), clearly empower the Commission to prescribe for Penn Water the power pooling and rate formula appropriate thereto here involved. Section 205 (a) of the Act's Part II relating to public utilities declares that "all rates and charges made, de-

manded, or received by any public utility" for sales which are subject to the Commission's jurisdiction³⁰ and "all rules and regulations affecting or pertaining to" them "shall be just and reasonable," and any of them that are not just and reasonable are "unlawful." Section 205 (b) forbids public utilities to "grant any undue preference * * * or [to] maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect."

Section 206 (a) empowers the Commission to enforce these provisions by expressly providing that if, after hearing, the Commission finds that "any rate, charge, or classification * * * or * * * rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory or preferential," it shall "determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and fix the same by order."³¹

³⁰ Penn Water's sales to Consolidated are concededly subject to the Commission's jurisdiction as sales for resale in interstate commerce (Penn Water's main brief below, p. 62). And as we show *infra*, pp. 105-117, Penn Water's sales for resale to its Pennsylvania utility customers are likewise in interstate commerce.

³¹ The Act also provides in Section 207 that whenever the Commission, upon complaint of a State Commission—after notice and opportunity for hearing—shall find that "any interstate service of any public utility is inadequate or insufficient, the Commission shall determine the proper, adequate, or sufficient service to be furnished, and shall fix the same by its order, rule, or regulation: * * *"

Not only was the Commission empowered to prescribe just and reasonable rates and services, but Congress made clear its intent that the Commission in so doing was also to bend its efforts to achieve "the most efficient use of the nation's resources consistent with the public interest in cheap power and in conservation" (R. XVIII, 5378). Section 202 (a) provides that the Commission shall have the duty "to promote and encourage" the "voluntary interconnection and coordination of facilities for the generation, transmission, and sale of electric energy" so as to assure "an abundant supply of electric energy throughout the United States with the greatest possible economy and with regard to the proper utilization and conservation of natural resources." And for this purpose, the Commission is "empowered and directed to divide the country into regional districts" (Section 202 (a)). In addition, the Commission is authorized by Section 202 (b), on application, to direct a public utility "to establish physical connection of its transmission facilities with the facilities of one or more other persons engaged in the transmission or sale of electric energy, to sell energy to or exchange energy with such persons," and to "prescribe the terms and conditions of the arrangement to be made between the persons affected by any such order, including the apportionment of cost between them and the compensation or reimburse-

ment reasonably due to any of them." Although in this case the Commission was not proceeding under Section 202 it properly took into account the congressional policy therein expressed in determining what rates and services should be prescribed (R. XVI, 5184).³²

³² The legislative history of Section 202 makes clear that, at least as far as the draftsmen were concerned, the objective of encouraging the coordinated use of power facilities sought to be achieved by that Section was one of the primary purposes of Part II. Cf. *Connecticut Light & Power Co. v. Federal Power Commission*, 324 U. S. 515, 525. Dozier A. DeVane, then Solicitor of the Commission, testified before the Senate Committee upon behalf of the bill of which he was the draftsman (Hearing before the Senate Committee on Interstate Commerce on S. 1725, 74th Cong., 1st Sess., p. 273):

"To my mind, that is one of the most important provisions of this bill. When you visualize what you are going to do by title I, that you are going to tear down the fences, which are the holding companies, and you are going to turn the operating utilities loose insofar as their prior control and ownership is concerned, that section takes on an added significance. It should be considered along with section 205 [now 203], which requires Commission approval for the purchase and sale of operating properties—to say where these properties shall go in the public interest. Under this bill, and without tremendous force of regulation on the part of the Commission, these companies will integrate into strong regional systems, as directed by Congress.

"What is the other great advantage to be gained by that? The advantage through proper interconnection of these properties of a substantial reduction in stand-by facilities. Where you have a system that has to depend upon its own generating facilities for its power you will find that in a great many instances the cost of stand-by facilities runs above 40 percent of the total cost, and you will find in a majority of instances that it will run between 30 and 40 percent. Studies have

Broad authority over rates and services is similarly vested in the Commission under Part I relating to licensees. Section 20 of that Part requires that "the rates charged and the service rendered by any * * * licensee [whose power enters interstate commerce] * * * shall be reasonable, nondiscriminatory, and just to the customer and all unreasonable discriminatory and unjust rates or services are hereby prohibited and declared to be unlawful; * * *." Section 20 goes on to provide that when the states directly concerned have failed to provide a com-

been made that convince a great many engineers and a great many other qualified people whose views are entitled to respect that with proper integration that investment can be reduced to approximately 15 percent. If the average is between 30 and 40 percent today, and if by integration we can reduce it to 15 percent, think of the benefit that will accrue to the consumers of this energy as the result of the establishment of regional districts and the proper interconnection of all facilities in each district."

And Frank R. McNinch, then Chairman of the Commission, stated in hearings before the House and Senate Committees considering the legislation, that Part II was

"* * * directed primarily toward the coordination of the power generated and transmission facilities in the United States, intended as we believe, effectively, to serve the interests of the consumer in bringing to the consumers electricity upon more economical terms and at less cost than under the present lack of coordinating arrangements and likewise being equally to the interest of the companies. [Hearings before the House Committee on Interstate and Foreign Commerce, 74th Cong., 1st Sess., on H. R. 5423, p. 383.]"

See also: *id.*, pp. 384, 517, 531, 535, 2165-2168; Hearings before the Senate Committee on Interstate Commerce, 74th Cong., 1st Sess., on S. 1725, pp. 257-258.

mission or the states are unable to agree,³³ "jurisdiction is hereby conferred upon the commission * * * to enforce the provisions of this section, to regulate and control so much of the services rendered, and of the rates and charges of payment therefor as constitute interstate or foreign commerce. * * *."

The Commission is further authorized to "issue such order as it may find appropriate, expedient, and in the public interest to conserve and utilize the * * * water-power resources of the region" (Section 4 (g)). Its power to issue licenses for the "development, transmission, and utilization of power * * * from * * * any of the streams * * * over which Congress has jurisdiction" (Section 4 (e)) is conditioned on the requirement that "the project * * * shall be such as in the judgment of the Commission will be best adapted to a comprehensive plan * * * for the improvement and utilization of water-power development" (Section 10 (a)).

The Commission's requirements as to power pooling and the residual method of payment are plainly within these broad grants of authority to prescribe and fix just and reasonable rates, charges and services. As we have shown *supra*,

³³ We show *infra*, p. 118, that the Commission's finding that the states here involved are unable to agree is conclusive here. It is not only supported by substantial evidence as ruled by the court below, but petitioners do not attack it.

pp. 11-15, because of the variable nature of the flow of the Susquehanna River and the limited storage capacity of its dam, Penn Water would be uneconomic as an independent unit. It would be unable to assume any substantial firm obligations. It would be unable to compete successfully with steam generating plants and, in periods of high flow, it would have to waste substantial amounts of water over the spillways.

On the other hand, by their integration with Consolidated's steam power generating facilities and large utility load, the most effective and economic use of Penn Water's hydro facilities can be—and has been—made. For example, Penn Water has been able to assume substantial firm obligations. When the flow is low, its facilities are used for peaking, thereby contributing maximum generating capacity when most needed and saving costs of using the oldest and most inefficient steam plants of the pool. And when the flow is high they are used to carry the system's base load, thereby reducing fuel costs and minimizing water waste.

By virtue of these arrangements, the "operations of Penn Water, Safe Harbor and [Consolidated] are closely integrated and coordinated as a matter of economy, efficiency, flexibility, and maximum utilization of hydro capabilities" (R. XVI, 4849), and the energy used to satisfy the demands of the customers of either Penn Water

or Consolidated is determined on the basis of maximum utilization and economy. These considerations more than justified the Commission's conclusion that (R. XVI, 5184):

The regional integration and coordination of facilities, the resulting economies, and the utilization and conservation of natural resources thus achieved are precisely what was sought to be encouraged and fostered by the Federal Power Act and established as a part of the criterion of the public interest to be served by regulation thereunder (Cf. Section 202 (a)).

The residual method of payment, including the system of entitlements, was likewise within the Commission's authority. Section 206 authorizes the Commission to fix "the just and reasonable rate * * * practice, or contract to be thereafter observed." And Section 20 requires only that the rate shall be "reasonable, nondiscriminatory, and just." Far from limiting the Commission's authority to prescribing rates on what Penn. Water describes as the "usual unit rate basis" *i. e.* on the basis of a fixed amount for a specified unit of service (Pet. in No. 428, pp. 15-16), these Sections permit the Commission to prescribe the rate in any form which in the circumstances of the particular case will be just and reasonable.

Because of the nature of the pooling arrangements whereby the supplying of energy is deter-

mined with the view of achieving maximum economies and optimum utilization of the available facilities, it would be difficult, if not impossible, to fix a rate on the unit basis which could be said with any assurance, to result in a specified over-~~all~~ return. For there are too many uncontrollable variables to be considered in forecasting the units of service Penn Water would furnish Consolidated over a given period of time, and that figure is basic to the fixing of a rate which will yield a given return.³⁴ In contrast to the difficulties of formulating a unit rate, the residual method payment prescribed by the Commission assures Penn Water that it will receive the 5 $\frac{1}{4}$ % return which the Commission found just and reasonable here—an end result which plainly satisfied the requirements of Sections 20 and 206. *F. P. C. v. Hope Natural Gas Co.*, 320 U. S. 591.

Not only does the method of payment prescribed meet the requirements of these Sections but the record before the Commission reveals that it is the only method of payment by which

³⁴ There would be, in addition, technical difficulties to fixing rates on a unit basis. As stated by George W. Spaulding, then Penn Water's vice-president and now its president (R. I. 75):

"Not only would the problem of segregation and classification of capacity and energy services be difficult, if not impossible, on the basis of metered quantities, but arbitrary assumptions in that respect would not always conform either with facts or the equities of the situation."

the full benefits of the power pool can be obtained. As shown, *supra*, pp. 15-19, Penn Water's several efforts to use the unit rate in various forms in each instance prevented the achieving of the pool's full benefits, for under this type of rate, it was to the interest of each of the parties to foster the use of its own facilities or energy entitlements irrespective of whether it resulted in over-all economies. Under the unit type of rate, therefore, the self interest of the individual parties stands as a strong deterrent to maximum economy in the use of their combined facilities. The Power Commission's formula rate, by providing for payment independently of whose power is used, eliminates the barrier to such economy created by conflicting self-interests. The Commission's formula fosters maximum utilization of Penn Water's hydro power. It also permits Penn Water to enter into firm commitments for delivery of power, which Penn Water, standing by itself, could not do because of variations in its power output resulting from the extreme variations in river flow.

The Commission's requirements that the power pooling and the residual method of payment by which these results were achieved, be continued are, therefore, clearly within the authority vested in it by Congress under the Federal Power Act.

II

**THE COMMISSION'S ORDER IS NOT INVALID BECAUSE OF
CONFLICT WITH THE ANTITRUST LAWS OR THE ANTI-
TRUST PROVISION OF THE FEDERAL POWER ACT**

**A. THE COMMISSION'S ORDER PRESCRIBING ARRANGEMENTS BE-
TWEEN PENN WATER AND CONSOLIDATED IS NOT SUBJECT TO
THE ANTITRUST LAWS**

*1. Arrangements validly prescribed by the Commission con-
stitute governmental action exempt from the antitrust laws*

The complete answer to petitioner's contention on this aspect of the case—an answer which would be dispositive of Nos. 611, 612 as well—is that the Commission's order is not subject to the antitrust laws. The Commission is not here approving or permitting private combinations, consolidations, or contracts which might otherwise contravene the Sherman Act. As to such matters the Government has consistently maintained that express statutory authority and an exercise of that authority are needed to establish an exemption from the antitrust laws. E. g., *United States v. Borden Co.*, 308 U. S. 188. The statutes authorizing agencies to exempt conduct from the antitrust laws³⁵ cited in the Appendix to Penn Water's brief are principally of this character; they authorize the granting of permission to private parties to do what might otherwise be illegal.

³⁵ Such as the amendment to Section 7 of the Clayton Act (15 U. S. C. (Supp. IV) 18), which exempts acquisition of assets authorized by the Power Commission.

But we are here concerned not with a private contract, combination or conspiracy, but with a governmental order binding of its own force apart from any contract. Absent any contract, the order would still stand. Violation of the order would be subject to the penalties of the Federal Power Act. Sec. 316. Conduct so ordered by a governmental agency acting within the scope of authority granted by Congress has *never* been held to violate the antitrust laws. Nor has the order itself—and it is the Commission's order which petitioners are attacking here. Since the Sherman Act does not apply to governmental action, we are not here confronted with any problem of implied repeal of the Sherman Act or as to whether the Federal Power Act is consistent with or repugnant to it. The words "restraint of trade" in that statute do not reach orders of government officials, or, of course, conduct taken in compliance therewith to avoid penalties imposed by the Government. So long as the Federal Power Commission was acting within the bounds³⁶ of the power granted to it by the Federal Power Act, as we have shown ~~to~~ (pp. 39-48, *supra*), the antitrust laws cannot affect this case.

The reasoning and principles of *Parker v. Brown*, 317 U. S. 341, which involved a situa-

³⁶ We need not consider here whether the antitrust laws would apply to a governmental agency acting outside of its statutory authority.

tion closely analogous to the instant case require, we submit, the holding here that the Commission's order pursuant to the authority delegated to it is governmental action not subject to the antitrust laws.

Parker v. Brown concerned the validity under the Sherman Act of a marketing program for raisins established under the California Agricultural Prorate Act, which authorized the establishment, through action of state officials, of programs for the marketing of agricultural commodities so as to restrict competition among the growers and maintain prices in the distribution of their commodities to packers. The Prorate Act provided for an Agricultural Prorate Advisory Commission, which was to undertake the establishment of a pro rata marketing plan after holding public hearings upon a petition filed by ten producers and after making certain required economic findings.³⁷ A program committee of producers selected by the State Director of Agriculture then formulated a program which the Commission after holding further hearings could modify and approve. If, thereafter, the requisite percentage of producers consented, the program was put into operation by the program

³⁷ That the institution of a program for the proposed zone will prevent agricultural waste and conserve the agricultural wealth of the state without permitting unreasonable profits to producers.

committee with violations thereof being subject to civil and criminal penalties.

Despite the very restrictive impact of the raisin program upon competition in interstate commerce—an effect which was undoubtedly intended and which would certainly have violated the Sherman Act if not governmental—this Court in *Parker v. Brown* unanimously ruled that the Sherman Act did not apply to the Prorate Act. The Court held that, although the producers had a voice in the program, its promulgation and operation constituted action by the State, and that since the Sherman Act was directed at outlawing private action, rather than regulatory action by a governmental body, the Act was inapplicable.³⁸

³⁸ A similar decision ¹⁵in *Olsen v. Smith*, 195 U. S. 332, in which this Court rejected the contention that a Texas law making the piloting of boats into the ports of Texas a State monopoly violated the Sherman Act, stated ¹⁶(195 U. S. at 344-345):

“The contention that because the commissioned pilots have a monopoly of the business, and by combination, among themselves exclude all others from rendering pilotage services, is also but a denial of the authority of the State to regulate, since if the State has the power to regulate, and in so doing to appoint and commission, those who are to perform pilotage services, it must follow that no monopoly or combination in a legal sense can arise from the fact that the duly authorized agents of the State are alone allowed to perform the duties devolving upon them by law.”

For State cases holding that the concept of monopoly is inapplicable to a state exercising its governmental functions, see *State v. Aiken*, 42 S. C. 222; *Utah Manufacturers' Association v. Stewart*, 82 Utah 198; *Guy v. Commissioners of Cumberland County*, 122 N. C. 471, and cases collected in Annotation 121 ALR 303.

This was not because the Prorate Act had superseded or impliedly repealed the Sherman Act, for California's law obviously could not have such effect, but because the restraint imposed by governmental order was not the kind of restraint which the Sherman Act reached.

Parker v. Brown, we submit, governs the instant case, for here, as in the *Parker* case, the action involved is that of a governmental regulatory body. Here, the Power Commission, acting pursuant to and within the delegation of authority by Congress, has prescribed certain relationships between Penn Water and Consolidated. The Commission has prescribed the rate schedule and has directed the continuance of the pooling arrangement and the residual method of payment. The companies are required to observe the prescribed order not because they have contracted to do so, but because the Commission has ordered it, irrespective of their contract. The charging of any rate or rendering of any service other than those prescribed by the Commission would constitute a violation of the Federal Power Act and would subject at least Penn Water to criminal penalties (Sec. 316 of the Power Act).

Plainly, therefore, the arrangements prescribed by the Commission "derived * * * [their] authority and * * * efficacy from the legislative command of the * * * [Commission acting under the authority delegated to it by Congress] and * * * [were] not intended to

operate or become effective without that command” (317 U. S. at 350). “It is the state, acting through the Commission which adopts [the requirements imposed by the Commission] and which enforces [them] with penal sanctions in the execution of a governmental policy” (317 U. S. at 352). “The state * * * made no contract or agreement and entered into no conspiracy in restraint of trade or to establish monopoly but, as sovereign, imposed the restraint as an act of government which the Sherman Act did not undertake to prohibit” (*ibid.*).

Indeed, the Commission’s orders here are even more clearly governmental action than the raisin proration program in *Parker v. Brown*; for in *Parker v. Brown*, the producers had a voice in the program—they not only had to consent to its going in effect but a committee of producers administered it; here, on the other hand, the Commission’s action is operative, irrespective of whether the consent of Penn Water or Consolidated is forthcoming.

The fact that we have federal, rather than state, action, far from making *Parker v. Brown* inapplicable here, as Penn Water suggests (Br. in. No. 428, pp. 39–40), makes the instant case even plainer. For it was, at least, arguable—and in fact argued in that case—that the congressional policy expressed in the Sherman Act should bar a State from eliminating competition and con-

trolling the price and supply for a product marketed throughout the Nation.³⁹ But this could not be said of a regulatory statute passed by Congress itself.⁴⁰ The Sherman Act's purpose and legislative history no more suggest a purpose to restrain Federal action than State action, and the Court's summary of the legislative history to the effect that the Act's "purpose was to suppress combinations to restrain competition and attempts to monopolize by individuals and corporations" (317 U. S. at 351) equally indicates its inapplicability to action by the Federal government.⁴¹

As *Parker v. Brown* points out (p. 351), this does not mean that a state can authorize private persons to enter into voluntary agreements to do what the Sherman Act prohibits. And the same is true of Federal agencies unless the statute makes such authority clear. That is all that the cases cited by petitioner (Br. in No. 428, pp. 29-32) hold. But since the Sherman Act reaches

³⁹ The Government's brief conceded that the Sherman Act would not, however, affect state regulation of utility rates. Brief for the United States as amicus curiae in No. 46, October Term, 1942, p. 64.

⁴⁰ Obviously, the United States itself cannot be a defendant in a Sherman Act case; it cannot even be a plaintiff in a treble damage suit, though a state may (*United States v. Cooper Corp.*, 312 U. S. 600; *Georgia v. Evans*, 316 U. S. 159).

⁴¹ For more elaborate reviews of the Sherman Act's legislative history and the common law principles on which it is based, see, e. g., *Aper Hosiery Co. v. Leader*, 310 U. S. 461, 492-8 and n 15; *Standard Oil Co. v. United States*, 221 U. S. 1, 51-59; *United States v. Addyston Pipe & Steel Co.*, 85 Fed. 271 (C. A. 6), affirmed, 175 U. S. 211.

only private contracts, it does not extend either to governmental orders or to private conduct undertaken in compliance with such orders.⁴²

2. *The antitrust laws do not apply to rates fixed by the Federal Power Commission*

It should not be forgotten that in this case we are dealing with a rate order. The Commission's initial order in this case merely required a reduction in rates. Its final order, prescribing the rates schedule, was likewise concerned only with rates, the method of computing rates and the services to be performed in return for payments to be paid (see pp. 70-72, *infra*). The last two items are clearly essential parts of a rate schedule, and must be considered in the rate-fixing process since the definition of a rate necessarily includes how it is to be computed and the services in return for which it must be paid.

Although private agreements with respect to rates in regulated industries are subject to the antitrust laws, it has been uniformly accepted for many years that the rates themselves are subject to the control of the regulatory agencies

⁴² We do not mean to suggest that a state may by mandatory statute provide that private interests shall not compete or shall agree voluntarily about prices or follow a parallel price policy (*Schwegmann Bros. v. Calvert Distillers Corp.*, 341 U. S. 384, 389), although Congress could if it so desired. But a state can fix prices itself; that is what we have here, and the kind of situation which we are considering in this brief.

under the applicable statute.⁴³ As stated in *Keogh v. Chicago & N. W. Ry. Co.*, 260 U. S. 156, 162:

What rates are legal is determined by the Act to Regulate Commerce.

See also *Georgia v. Penn R. Co.*, 324 U. S. 439, 453-455, and cases cited. And the same is obviously true as to the Federal Power Act. *Montana-Dakota Utilities Co. v. Northwestern Public Service Co.*, 341 U. S. 246, 251.

Citation is not necessary to show that in determining "just and reasonable" rates, the standard under almost every statute, the agency may weigh many factors in addition to antitrust criteria. Even though the general policy in favor of competition is one factor which must be considered (*McLean Trucking Co. v. United States*, 321 U. S. 67, 86, 87), in general, as the court below stated, with respect to rates the determination of "just and reasonable" is governed not "by the pressures of competition [or the lack of it] but by the adequacy of the service to the

⁴³ *Keogh v. Chicago & Northwestern Ry. Co.*, 260 U. S. 156; *United States Navigation Co. v. Cunard Steamship Co.*, 284 U. S. 474, 485; *Central Transfer Co. v. Terminal R. Assn.*, 288 U. S. 469; *Terminal Warehouse v. Pennsylvania R. Co.*, 297 U. S. 500, 514; *McLean Trucking Co. v. United States*, 321 U. S. 67, 83; *Georgia v. Pennsylvania R. Co.*, 324 U. S. 439; *Far Eastern Conference v. United States*, decided March 10, 1952. See also, *S. S. W., Inc. v. Air Transport Association*, 191 F. 2d 658, 661 (CADC) pending on petition for writ of certiorari, No. 568, this Term.

public, the fairness of the return allowed upon the investment in the company and the degree to which the congressional objective of efficient use of the nation's power resources is served" (R. XVIII, 5372). Cf. *Federal Power Commission v. Hope Natural Gas Co.*, 320 U. S. 591, 603.

The need for regulation of the rates of public utilities arises in large part because experience has demonstrated that such industries cannot be fully competitive and that competition will not adequately protect the public. Because of economic and technological facts electric utilities are in large measure natural monopolies. Prior to the enactment of the Federal Power Act in 1935, various evils had developed in the electric utility industry which could not be effectively dealt with under the laws as they then existed—which, of course included the antitrust laws—and the Power Act, together with the Public Utility Holding Company Act, was directed at these evils. See *Federal Power Commission v. Hope Natural Gas Co.*, 320 U. S. 591, 609. Thus, "in place of competition as a generalized and indirect regulator of prices and services", for the "field of interstate transmission of electric energy at wholesale" (R. XVIII, 5371), Congress has provided for regulation by the Federal Power Commission of certain phases of utility activities, including the fixing of rates and services, to protect the public-interest against, *inter alia*, the

very evils attending monopolistic control at which the Sherman Act is directed.

In this field of rate regulation the Commission is not precluded from prescribing arrangements which might be unlawful under the Sherman Act, if contained only in private agreements. This can be demonstrated by a simple example. Two utilities cannot legally agree upon the rates they will charge customers. But a regulatory commission can *prescribe* the same rates for each—and neither the agency nor the companies which obey this order will be in violation of the antitrust laws. So long as the order is authorized by the regulatory statute, it is valid—and there is no need for any express statutory provision stating that the antitrust laws are not an implied limitation upon the agency's statutory rate-making authority. This would seem to be the theory and philosophy underlying such cases as *Keogh*, *Terminal Warehouse*, *Georgia* and *Far Eastern Conference*.

It is true that in the cases cited the rates were sought to be challenged collaterally, whereas this case (as distinct from Nos. 611 and 612) is a direct review of the order of the regulatory agency. But the governing principle is still the same—rates which conform to the standard of the regulatory statute are not governed by the antitrust laws.

This principle is sufficient to dispose of the instant case. For, as we have shown, the Commission's order is a rate order. Inclusion within it of provisions as to the continued pooling of power resources relates to the service to be rendered in return for the rates to be fixed, is obviously necessary if the power of the Susquehanna is to be effectively utilized, and in any event is not challenged here as unlawful. This means that it was entirely proper for the Commission to require Penn Water to continue to dispose of its power by selling Consolidated the residue, as part of an arrangement whereby Consolidated transmits steam generated energy to Penn Water when the water power is insufficient to supply the firm demands of the latter's Pennsylvania customers. Once this method of providing service is accepted, it is apparent that the residual method of determining the amount Consolidated must pay Penn Water is merely a rate formula adapted to the service for which the rate is being fixed, and thus within the Commission's power to prescribe just and reasonable rates.

There can be no doubt as to the reasonableness of the residual payment formula in the present circumstances." The joint operation of Penn

"We do not doubt that in ordinary industry an agreement between competitors whereby one both guarantees and limits the other's profits, thus depriving the latter of its incentive to compete, would violate the antitrust laws where the effect would be substantially to lessen competition in the industry

Water's hydro facilities and Consolidated's steam plants enables Penn Water to provide a substantial portion of the power needed in a large and populous territory in Maryland and Pennsylvania, whereas unless Penn Water's resources were supplemented by large steam power capacity, it could not serve as a source of firm power supply to any area of more than minuscule size. Such joint operation of the plants, as a single system in which power could flow from one to the other as required by the amount of water in the Susquehanna, would best serve the public interest in cheap power if the sole consideration on the part of the operators of the system were the economical production of electric energy. But if each company were required to pay for each unit of power supplied by the other, each would have an incentive to sell as much of its own power and to receive as little of the other company's as possible. The experience of these two companies prior to 1931, under just such a plan, revealed its deficiencies, and resulted in the adoption of the residual method of payment. See pp. 15-19, 47-48, *supra*.

If Penn Water were required to stand alone as an independent competitor, most of the value of concerned. In the particular circumstances of this case, however, where the method of payment is tied into a pooling of the product, electric energy, which is required by the physical nature of the source of the energy, the available flow of the Susquehanna River, a different result might be reached.

the water power would be lost. The public's interest in the most efficient and economical utilization of the water power of the Susquehanna would inevitably suffer if the hydro company were required to compete for revenue with the very steam plants with which its facilities were physically and economically joined.

When the reasonableness of the method of payment from the standpoint of the public interest in low power rates (pp. 11-19, *supra*) is considered in connection with the statutory authority of the Federal Power Commission over rates and charges, which includes, of course, the method of computing them (pp. 39-48, *supra*), it is clear that the payment provisions of the order fall within the area of the Commission's discretionary authority over rates, and that there is no occasion to consider whether a private arrangement of the same sort would violate the antitrust laws. The provisions of the Commission's order prescribing the service to be rendered and the method of paying for them are thus a proper exercise of the power to regulate rates and are not violative of the antitrust laws. The other provisions of the order, including those incorporated by reference from the prior contract, are merely ancillary to the regulation of rates and services. As we shall see in Point II C, *infra*, pp. 65-73, these ancillary provisions do not include the two articles of the

prior contract found by the Fourth Circuit to be unlawful under the antitrust laws.

B. THE COMMISSION'S ORDER DOES NOT VIOLATE SECTION 10 (H)
OF THE POWER ACT

Petitioners also assert that the Commission's order and the contracts upon which they allege it is based are in violation of the antitrust provision contained in Section 10 (h) of the Federal Power Act. Section 10 provides that:

All licenses issued under this Part shall be on the following conditions:

* * * * *

(h) That combinations, agreements, arrangements, or understandings, express or implied, to limit the output of electrical energy, to restrain trade, or to fix, maintain, or increase prices for electrical energy or service are hereby prohibited.

The court below rejected petitioners' contention on the ground that since Section 10 (h) was contained in Part I of the Power Act, it did not apply to utilities also covered by Part II, and that, if necessary, Part II should be construed as having superseded Section 10 (h) for utilities subject to that Part (R. XVIII, 5377-5379).

We do not believe that Section 10 (h) has been repealed or superseded by Part II, or that it is necessary so to hold to determine this case. Section 10 (h) is one of the conditions attached to the license of a company which operates a project

on a navigable stream or on public land, pursuant to the permission granted by Part I. For violation of any of the conditions, including that contained in paragraph (h), the license is subject to revocation through a suit instituted by the Attorney General. Section 26. The condition imposed by Section 10 (h) would seem to be binding on companies subject to Part I even if they are also subject to regulation under Part II.

But on its face Section 10 (h) has the same scope as the Sherman Act itself. When it refers to "combinations, agreements, arrangements, or understandings," it is obviously concerned only with private combinations, etc., just as is the Sherman Act (pp. 49-56, *supra*). Section 10 (h) thus clearly does not interfere with or diminish the authority of the Commission to issue rate orders, and does not make it unlawful for licensees to comply with orders which the Commission has validly prescribed. The argument in Point II A, pages 49-63, *supra*, which demonstrates that such orders and conduct taken in compliance therewith do not violate the Sherman Act, is equally applicable to Section 10 (h).

Accordingly, if it be assumed that Penn Water, as a licensee subject to regulation under Part I and a wholesaler in interstate commerce subject to regulation under Part II, is still bound by Section 10 (h), its position in this case will not

be advanced. For Section 10 (h) does not invalidate the Power Commission's order prescribing the rates and services to be performed. Since the Power Commission has not authorized the continuance of any private agreement, in restraint of trade or otherwise, but has prescribed rates of its own, it is obvious that a statutory provision prohibiting only certain types of private agreements or combinations has no application.

C. THE COMMISSION HAS NOT ORDERED THE CONTINUANCE OF ANY CONTRACTUAL PROVISION HELD UNLAWFUL BY THE FOURTH CIRCUIT OR OTHERWISE UNLAWFUL

1. *The Fourth Circuit held only Articles IV and V of the Penn Water contract, not the pooling and residual payment provisions, to be unlawful*

A basic premise in the petitioners' argument is that the Commission's order is in conflict with the decision of the Fourth Circuit because the Commission prescribed contractual provisions held by the Fourth Circuit to be unlawful. This Court is, of course, not bound by the Fourth Circuit's ruling—as petitioners themselves recognize in attributing antitrust violations to provisions of the contract which the Fourth Circuit clearly did not hold to be unlawful. See pp. 74-75, *infra*. In view of the petitioners' strong reliance upon the Fourth Circuit's decision, however, it is important to ascertain precisely what provisions of the contract that court held to be un-

lawful.⁴⁵ Such an inquiry, followed by a reference to the terms of the Commission's order, will reveal that the Commission has not prescribed anything held unlawful by the Fourth Circuit, as that court itself agrees.

The Fourth Circuit's opinions demonstrate plainly that only Articles IV and V of the agreement were held to be "illegal restrictions" in violation of the antitrust laws. These are the articles which prevent Penn Water from entering into contracts of sale or purchase and from expanding or contracting its plant without Consolidated's consent. (See p. 10, *supra*; R. XV, 4612-4613, R. XVIII, 5328.) These provisions the Fourth Circuit characterized throughout its opinions as the "illegal restrictions."

The court discusses these provisions and their effect in detail, and concludes that they violated the antitrust laws (R. XVIII, 5330-5331). But there is no suggestion in any of the Fourth Circuit's opinions that the provisions of the contract relating to power pooling and method of payment were unlawful, and this despite the fact that Penn Water urged (see Br. in first *Consolidated* case in the Fourth Circuit, p. 27), as it does here

⁴⁵ We do not mean to suggest or concede that the Fourth Circuit possessed jurisdiction to invalidate any provisions of a Commission rate order, including any which may have been effectuated by reference to a contract filed as a rate schedule. The Commission rather than the court would seem to have primary jurisdiction over attacks upon the validity of anything which the Commission has prescribed.

(Br. in No. 428, pp. 63-67), that the payment provisions also violated the antitrust laws. On the contrary, the court repeatedly described the contract in terms which demonstrate that it regarded the provisions relating to power pooling and payment, but not Articles IV and V, as entirely lawful. Thus in the Fourth Circuit's second opinion (R. XVIII, 5358) it described the Penn Water-Consolidated contract as providing that:

Consolidated should be entitled to all of the electric capacity and energy available to Penn Water and not otherwise disposed of in the performance of existing contracts, and in consideration thereof, Consolidated agreed to pay Penn Water an amount equal to its operating expenses, a specified rate of return on existing facilities, and on the cost of new facilities less depreciation, * * * *Closely associated with these provisions were the illegal restrictions on the future activities of Penn Water which resulted in the invalidation of the whole contract. [Italics supplied.]*

Substantially the same language was employed in the court's prior reference to the Third Circuit's *Safe Harbor* decision, when after referring to the provisions for disposal of the supply of electric energy and the method of payment therefor, the court said (R. XVIII, 5343):

The restrictive provisions of the agreement were not mentioned and their legal validity was not discussed.

That the Fourth Circuit so construed its decision in the case involving the Penn Water-Consolidated contract is confirmed by the opinion in the second *Consolidated* case, which states flatly that the contract had been held "invalid.[in the first case] because Articles IV and V * * * conferred upon Consolidated the power to control" Penn Water's activities (No. 611, R. 233, slip op., pp. 3-4). The court went on to describe the contract in the instant case as providing in effect that Consolidated should be entitled to Penn Water's power in return for paying its operating costs and a specified greater rate; "and then", said the court, "followed the illegal restrictions upon the activities of Penn Water" (No. 611, R. 234-235, slip op., p. 5).⁴⁶

These repeated statements by the Fourth Cir-

⁴⁶ Petitioners' argument (Br. No. 428, p. 63 fn.) that the Fourth Circuit held unlawful the payment provisions of the contract here involved is contrary to the entire tenor of the opinions in the first *Consolidated* case there, as well as to the passage from the second case quoted in the text. Petitioners advert, however, to the fact that at one point in its opinion in the second *Consolidated* case the Fourth Circuit seems to have included the pooling and payment provisions of the contract there involved among those which it classified as "restrictions" (No. 611, R. 235-236, slip op., pp. 6-7). But this seems inconsistent with the passage quoted in the text from the same opinion, and the opinion as a whole also indicates clearly that the court is only holding particular restrictive articles of the contract there involved to be unlawful. In any event, in the passage to which petitioners refer, the Fourth Circuit was not referring to the payment provisions in the contract in the instant case.

cuit which contrast the pooling and payment provisions with the "illegal restrictions" leave no possible doubt that the only provisions of the Penn Water-Consolidated contract which it held violative of the antitrust laws were the restrictions contained in Articles IV and V. The court went on to invalidate the entire contract, including the provisions relating to the power pooling and the method of payment, but not because it regarded the latter provisions as illegal in and of themselves; this was never suggested. The reason was that the court deemed Articles IV and V to be so inseparable from the remainder of the contract that without these Articles the latter could not be said to reflect the intention of the parties and hence could not function as an agreement between them (R. XVIII, 5358-5359). Despite this invalidation of the entire contract, there is no suggestion in the Fourth Circuit's opinion of any legal obstacle which would have prevented the parties from entering into another agreement in effect reaffirming the earlier contract minus, of course, the illegal articles. By the same token, nothing suggests that if the Commission were to prescribe the continuance of such arrangements minus the restrictive provisions there would be any violation of the antitrust laws. That is what the Commission did.

2. *The Commission did not prescribe any unlawful provisions of the contract*

Although, as Penn Water points out in its brief (No. 428, p. 49), the Commission referred to Articles IV and V in its opinion on rehearing (R. XVI, 5184), nothing in that opinion or the other opinions or orders entered in this case directs the continuance of those provisions.

In its original order of January 5, 1949, before Penn Water had raised the antitrust objection, the Commission did not order compliance with the terms of the contract generally, or refer to Articles IV and V at all. The Commission at that time merely ordered that the formula payment arrangement "whereby sales to Pennsylvania customers are made on a firm basis on definite rate schedules whereas Baltimore Company takes what is left and assures" Penn Water of the "recovery of all proper operating expenses * * * and a fair return" be continued at greatly lowered rates (R. XVI, 4981, 4994). It did not prescribe the provisions of any contract or rate schedule, but ordered Penn Water to file "a new schedule of rates and charges" which would effectuate the rate reduction (R. XVI, 4995). When confronted for the first time, on petitioners' first petition for rehearing, with Penn Water's claim that Articles IV and V were illegal, the Commission referred to the above quoted portion of its prior opinion, and commented (R. XVI, 5184-5185) that:

If there are questions as to the legality of the foundation contracts which are in litigation, as Respondents' application for rehearing indicates the validity of our order is not dependent upon the decision of those questions. In our opinion and order, we took care to leave the continuation of the operation of the integrated and interconnected system in full effect, merely changing the rates * * *.

Thus, the Commission made it clear that it did not regard its own order as prescribing anything except a reduction in rates computed in substantially the same manner as provided in the contract.⁴⁷

Only when it concluded that Penn Water would not file a satisfactory schedule of rates and charges did the Commission itself prescribe its own rate schedule (R. XVII, 5277-5283), and also order that (R. XVII, 5283)—

All other provisions of the aforementioned contracts, *in and of themselves lawful*

⁴⁷ The assertion that the Consolidated contract is inseparable and "is not a rational business arrangement" without Articles IV and V (No. 428, Br., p. 59, fn.) obviously has no bearing on whether the Commission prescribed such an arrangement. For the Commission's duty is to require arrangements which further the public interest without regard to whether private business concerns, acting pursuant to their individual interests, would voluntarily assume similar obligations. The "inseparability" found by the Fourth Circuit in the contract *qua contract* depended on the intention of the parties, and clearly would not extend to the Commission's order which is not dependent upon private intent.

prescribing or defining in the power, energy and transmission services to be furnished, or any classification, practice, regulation or rule affecting such services, which several provisions are incorporated herein by reference, shall be observed and be in force.

The Commission was, at the time fully aware of the claimed illegality of these provisions (see pp. 24-25, *supra*) ; accordingly, it limited its prescription to provisions "in and of themselves lawful" in order to insure that its order would not be construed as having prescribed any provision which might be held unlawful in the course of Penn Water's antitrust litigation against Consolidated. In addition, and significantly, the provision in question is limited to the portions of the contract "prescribing or defining the power * * * services to be furnished," or any rule "affecting such services"; it does not order compliance with the contract as such.

Both the Fourth Circuit and the court below have so understood the Commission's opinions. In the second *Consolidated* case, the Fourth Circuit rejected the Commission's assertion that in that case, unlike the first *Consolidated* case, it had prescribed the entire contract, including the restraints, largely because it agreed that the Commission had not done so in the first case, saying (No. 611, R. 243, Slip op., p. 15):

* * * It is obvious that the Commission did not prescribe the restrictive conditions of the contract as part of the rate order in either case * * *

Similarly the court below has not said that the Commission has prescribed the restrictive conditions; on the contrary, it has sharply differentiated between these restrictive provisions and the arrangements prescribed by the Commission pursuant to its authority under the Federal Power Act to prescribe reasonable rates and services. Thus, on the one hand, the court described the restraints in Articles IV and V as having "been privately agreed upon by the parties and submitted to the Commission as an accomplished fact" (R. XVIII, 5375). Cf. *Georgia v. Pennsylvania R. Co.*, 324 U. S. 439, 461-462. On the other hand, the court below points out that the Fourth Circuit, following the lead of this Court in the *Georgia* case, properly avoided affecting any pending rate proceeding; comments that the Commission's order relates only to "services and rates, reflecting underlying operations"; and rules that as such, its validity is governed by the Federal Power Act (R. XVII, 5375).

D. THE COMMISSION'S ORDER IS NOT BASED ON THE CONTINUANCE OF THE CONTRACT

Petitioners argue that the Commission's order is based upon continuance of the contract, that the Fourth Circuit held the entire contract in-

valid,⁴⁵ and that therefore the order must fall unless the Commission can override the Fourth Circuit's decision as to the validity of the contract under the antitrust laws. But the Commission's order did not rest on the contract as such, but on the preexisting method of operation. In ordering the continuance of that method so far as lawful, the Commission was not ordering continuance of the contract *qua* voluntary contract. The Commission's order prescribing rates, charges and services to be performed stands or falls irrespective of the contract or its validity as private arrangement—even though the order incorporated parts of the contract by reference.

Particularly insofar as the method of payment is concerned the Commission has superseded private contract provisions. In the rate schedule which it "prescribed" (R. XVII, 5277, 5279-5283) the Commission spelled out in full detail the manner in which the payments by Consolidated to Penn Water were to be computed. The Commission-prescribed order—four record pages in length (R. XVII, 5279-5283)—thus completely supplants the four-and-a-third pages of Article III of the original contract, which covers the same ground (R. XV, 4608-4612).⁴⁶ The fact that the

⁴⁵ As has been pointed out, the contract was held invalid because the court held the remainder inseparable from the restrictive provisions in Article IV and V.

⁴⁶ The original Article III was modified and slightly lengthened by the supplemental agreement of September 29, 1939 (R. XV, 4619-4621).

Commission's order followed in general the residual method for computing the payments employed in the prior contract does not mean that that portion of the contract was left in effect. The last paragraph of the Commission's "prescribed rate schedule" which incorporated by reference only "all *other* provisions of the aforementioned contracts, in and of themselves lawful" (R. XVII, 5283), makes this plain. For the preceding sentence states that:

The foregoing provisions supersede only the rates and charges heretofore made, demanded, collected or assessed against the Baltimore Company [Consolidated] by Penn Water * * *.

"The foregoing provisions" of the Commission order were those to which we have referred, which defined the method of computing the amount to be paid, and are obviously rate-making provisions. The fact that the method prescribed is more complex than usual does not make the prescribed schedule any less one concerned entirely with the fixing of rates.

Although we think that the point requires no further reply, it seems advisable to deal separately with each of the "critical features" of the order which petitioners assert to be based upon the assumed existence and continuance of the contract.

(1) *Interstate Commerce*.—Petitioners object that the Commission's finding that the sales to

Pennsylvania utility customers were in interstate commerce ^{was} ~~were~~ based on the provisions as to pooling contained in the invalidated contracts and must fall with the contracts. The Commission's jurisdiction over interstate sales, however, necessarily rests on the method of operation prior to the entry of the Commission's order and not on the contractual arrangements therefor. What else can the Commission look to as the basis for its jurisdictional finding? If the record before the Commission reveals that a power company's sales have been interstate up to that time⁵⁰—whether by reason of private contract or not, and irrespective of whether lawful or not—the Commission is authorized to regulate them. The possibility that by reason of the lapse of a private contract or otherwise the company may wish to change its method of doing business in the future so as to affect the interstate nature of a portion of its operations does not deprive the Commission of jurisdiction to regulate what has been interstate up to that time.

For at least 20 years Penn Water's facilities have been operated in conjunction with those of Consolidated, with the result that the power has flowed from Maryland to Pennsylvania cities, as well as from the dam in Pennsylvania to Baltimore. Despite the Fourth Circuit decision, this flow is still continuing. To alter it would doubtless require some rearrangement of physical plant,

⁵⁰ That Penn Water's sales were interstate is shown in Point V, *infra*, pp. 105-112.

as well as the consent of the proper regulatory authority.⁵¹ At least until that occurs, if it ever does, the Power Commission's authority continues irrespective of the contracts.

(2) *Rate of Return*.—Penn Water bases its claim that the 5¼% return fixed by the Commission was premised on the security afforded it by its contract with Consolidated (Br. in No. 428, p. 52-3), on references by the Commission to the fact that the contract assured it of a "stabilized income" (R. XVI, 4953) and by the court below to the evidence before the Commission that Penn Water was "insulated" from any "substantial risk" by the contract (R. XVIII, 5386):

The substitution of a Commission-prescribed arrangement for a contractual one of the same sort will provide the same stability of income for as long as the Commission-prescribed rates remain in effect. Only if one of the parties seeks and obtains permission to escape from the ar-

⁵¹ In discussing Penn Water's threat in its petition for rehearing to terminate its present services and undertake new services, the Commission has pointed out that any such change would require 30-day notice to be given by filing with the Commission new schedules of rates and charges which would afford Consolidated and the Maryland Commission an opportunity—

"to make application under Section 202 (b) for an order 'to sell * * * or exchange energy' from and after the time of the proposed change or termination of service; or a complaint under Section 207 as to the adequacy of the service to be rendered." (R. XVI, 5188; see also R. XVI, 5180-1, 5185-8.)

arrangement might there be any prejudicial change, which would then be taken into account in fixing a new rate. Nothing that has occurred to date suggests that any party but Penn Water itself is seeking such escape. Even the possibility that the arrangement might be terminated before the expiration date of the contract, 1980, would not impair the stability of income which Penn Water will receive under the method of payment prescribed by the Commission. Throughout whatever period the Commission-prescribed rates are operative, be it a month, a year, or a decade, they will for that period provide the same stability of income previously afforded by the contract-provided rates.

A reading of the Commission's order will disclose that the company's financial experience under the contract was only one of a number of factors which the Commission considered in fixing the rate of return. Equally emphasized was the ready market available for Penn Water's power, and the Baltimore company's sound financial position, all of which are equally beneficial to Penn Water so long as the present arrangement continues pursuant to the Commission's order, contract or no contract (R. XVI, 4953-4). Of principal importance, of course, was the Commission's view that a $5\frac{1}{4}\%$ return applied to the rate base and designed to provide 3.17% for bonds, 5.21% for preferred stock (Penn Water's actual pres-

ent costs) and 8.64% for common stock and surplus was "fair" (R. XVI, 4954-6). The court below has held that there was substantial evidence to support this conclusion (R. XVIII, 5387) and we do not understand petitioners any longer to urge the contrary.

(3) *Allocation of Rate Reduction.*—(a) Petitioners attack the Commission's allocation of the excess revenues as being improperly based on Consolidated's "entitlements" under the invalidated Consolidated and Safe Harbor contracts rather than on the power actually delivered (Br. in No. 428, pp. 55-58; Br. in No. 429, pp. 32-34). But this contention ignores the distinction pointed out *supra*, pp. 73-75, between the provisions of the invalidated contracts and the Commission's order, which superimposed upon Penn Water relationships with Consolidated which have existence independent of the contract. Since the Commission's order prescribing the payments to be made by Consolidated involved a formula for computing charges similar to that provided under the contracts,⁵² the Commission appropriately referred to the operation of the formula method under the contracts. The Commission, accordingly, included Consolidated's entitlements, which were to be continued under the terms of the order fixing the amount of the rate reduction to be

⁵² The Commission's formula, although following the general lines of the contract formula, differed therefrom in several important respects. See *supra*, p. 23, fn. 24.

allocated to Consolidated. And inasmuch as the credits for these entitlements were common to both the Commission's formula and that of the contract, the Commission computed the actual amount of the entitlements on the basis of the companies' experience in the test year of 1946. This does not, however, mean that the credits to which the Commission ruled Consolidated entitled resulted from the contracts or because the Commission felt bound by the terms of the contracts to allow these credits. On the contrary, Consolidated received the credits because they were due it under the formula prescribed by the Commission as the "most practicable under the circumstances" to achieve the maximum over-all economy and coordination of resources and facilities. (R. XVI, 4981.)

(b) Petitioners further argue that the Commission erroneously construed the Consolidated's entitlements under the contracts. This claim was expressly overruled by the court below (R. XVIII, 5392-5393) and has not been specified as error. The argument, which in effect is that the Commission could only prescribe those entitlements provided in the contracts, with any departure therefrom being invalid, is patently inconsistent with the contention just discussed. Here, again, it is important to remember that the Commission was not prescribing the continuance of the contract provisions as such, but rather imposing its own requirements. And with this distinction in

mind, it becomes clear that it is immaterial whether the Commission in fact misconstrued the entitlements under the contract. The Commission was not bound to follow the contract formula method precisely or even generally in prescribing the method of payment, and all it intended to do was to prescribe entitlements as it understood them to exist, but as in any event it ordered they should continue.

In any case, it is demonstrable that the Commission's allocation actually did follow that provided by the contracts. Petitioners attack principally the \$1,127,000 credit allowed Consolidated for the so-called economy interchange (Br. in No. 428, p. 57; Br. in No. 429, pp. 32-34). This credit arose from the fact that at those times when Consolidated's additional cost of steam generation is lower than that of a Pennsylvania utility, energy was furnished from the pool to Penn Water's Pennsylvania utility customers over and above its firm obligations to them. This energy, which was delivered by Penn Water, was obtained by diverting from Consolidated (1) the residual energy generated by Penn Water (i. e., the energy remaining after all of Penn Water's firm obligations are satisfied) to which Consolidated was entitled⁵³ and (2) part of Consolidated's entitle-

⁵³ Despite petitioners' present contention (Br. No. 428, p. 59 fn.; Br. in No. 429, p. 34), Penn Water has consistently recognized that Consolidated is entitled to all its energy remaining after its firm obligations had been met. See R. I, 50, 64, 65, 82, 489-490; II, 652; XV 4654.

ment to two-thirds of Safe Harbor total output;⁵⁴ in addition, Consolidated itself generated some of the energy used for this economy interchange. Thus, of the 191,664,000 Kwh furnished to Penn Water's customers on this basis in 1946, 65,863,000 Kwh was furnished directly by Consolidated and the remainder (125,801,000 Kwh) came out of Consolidated's residual and Safe Harbor entitlements. For the energy so furnished, Penn Water was paid a total of \$1,127,699, computed at a price based on sharing the savings involved (i. e., a price halfway between Consolidated's additional cost of generating⁵⁵ and the higher cost to the

⁵⁴ Penn Water's claim (Br. No. 428, p. 56), that the $\frac{1}{3}$ - $\frac{2}{3}$ division of Safe Harbor's output should have been applied after energy was furnished under contracts to which Safe Harbor was a party, is contrary to the construction given that contract in the proceeding in which it was directly involved. (*Safe Harbor W. P. Corp. v. F. P. C.*, 179 F. 2d 179, 184-185, fn. 9 (C. A. 3) certiorari denied, 339 U. S. 957). It is also contrary to the evidence in this proceeding, which shows that Safe Harbor was only a nominal party to these contracts for certain tax purposes (R. V, 2382, 2401-2) and that all the parties concerned regarded Safe Harbor's joinder in these contracts as not affecting Consolidated's right to $\frac{2}{3}$'s of Safe Harbor's entire output. (See e. g., R. XV, 4645-6, 4648-9, 4682-87; II, 608-10; X, 3715, 3720).

⁵⁵ To have computed the price on the basis of Safe Harbor's cost of hydro generation rather than Consolidated's cost of steam generation as suggested by Penn Water (Pet. Br. No. 428, p. 57, fn.), would have been unfair. Consolidated has to incur steam generating costs not only to furnish the economy interchange energy but to make up for the energy diverted from it. In these circumstances it is only equitable to compute the allowance on the basis of actual costs incurred, as the court below held (R. XV/II, 5392).

Pennsylvania utility if it had ~~not~~ generated). Inasmuch as the energy so sold belonged to Consolidated and in effect was for its account, Consolidated was clearly entitled to a credit therefor.⁵⁶ It is largely by virtue of this credit that Penn Water's excess revenues from Consolidated were increased from the \$700,900 actually received from Consolidated to about \$1,700,000.⁵⁷

(4) *The order prescribed by the Commission is independent of the restrictive provisions of the contract.*—Penn Water argues that the Commission's order prescribing contractual provisions is void because the "illegalities" contained in Article IV and V permeate the entire arrangement. We do not agree, for the order stands independently of the contract, and of Articles IV and V.⁵⁸ In so far as the order is concerned,

⁵⁶ The Commission included in Penn Water's cost of serving Consolidated, the costs Penn Water incurred in furnishing the economy interchange energy to the Pennsylvania utilities.

⁵⁷ The facts, that the Commission has prescribed the entire Safe Harbor contract and that the entitlements thus prescribed are involved in determining the rate reduction allocation, do not provide any basis for attacking the present order. See Point IV, *infra*, pp. 94-105.

⁵⁸ The phrase "with Electric's [Consolidated's] approval" contained in Article II (R. XV, 4607-4608) is the only other portion of the contract which would seem to be dependent upon the restrictive articles. The Commission no more prescribed this clause than it did Articles IV and V. This provision was plainly not prescribed by the Commission because it was fixing rates for Penn Water's services "as heretofore rendered," not for altered service to Consolidated in the event Penn Water entered into new contracts with other customers in the future (R. XVII, 5279; XVI, 4981, 5185).

Penn Water need not obtain Consolidated's consent before expanding or taking on new customers. If the new arrangements should affect the service rendered by Penn Water to Consolidated, Penn Water must file a new rate schedule for the changed service. If a new contract should render the arrangement presently prescribed by the Commission unfair to either party, it may apply to the Commission for a modification of the present order.

In any event, since the antitrust laws do not apply to the Commission's order (*supra*, pp. 49-63), it is immaterial whether any provisions of the order might violate the antitrust laws if viewed as private contractual arrangements. Even more clearly, therefore, the Commission's order is not invalidated because the contract as such may have been permeated with "illegalities".

III

THE POWER COMMISSION DID NOT PRESCRIBE CONTINUANCE OF ANY CONTRACTUAL PROVISION WHICH MIGHT CONCEIVABLY VIOLATE THE LAWS OF PENNSYLVANIA, AND IF IT DID THOSE LAWS WOULD NOT INVALIDATE ITS ORDER

Petitioners contend that the Commission's order violates not only the antitrust laws but the laws of Pennsylvania. The Fourth Circuit so held with respect to the restrictive conditions in the contracts in both of the antitrust cases.

A. THE POWER COMMISSION HAS NOT PRESCRIBED ANY CONTRACTUAL PROVISIONS WHICH WOULD VIOLATE THE LAWS OF PENNSYLVANIA

Petitioners assert that Pennsylvania law is violated because the contract destroyed both Penn Water's "independent corporate character" by divesting "the board of directors of powers of management" (Br. in No. 429, pp. 20-21) and depriving it of the powers to initiate "reasonable rates and adequate services" (Br. in No. 429, p. 21; cf. Br. in No. 428, pp. 68-72).

Obviously, only the restrictive conditions in Articles IV and V can have any such effect, and these were the only provisions which the Fourth Circuit held unlawful, as we have shown (pp. 65-69, *supra*). Since, as we have also demonstrated (pp. 70-73, *supra*), the Power Commission has not prescribed the continuance of those provisions, the order does not conflict with any of the Pennsylvania statutes cited. Those statutes, which insofar as the present issue is concerned, do no more than forbid directors to abdicate their authority, do not outlaw reasonable arrangements for the coordination of hydro and steam power facilities in the public interest or a cost-plus method of payment which would lead to more efficient and economical production of electric energy. We shall point out in subsection (C) of this Point, *infra*, pp. 90-93, how far the Pennsylvania statutes are from having any bearing on the instant case.

B. A RATE ORDER VALID UNDER FEDERAL LAW CANNOT BE
INVALIDATED BY THE LAW OF PENNSYLVANIA

Even if it be assumed that Pennsylvania statutes are inconsistent with the Power Commission's order, that order would stand as long as it was authorized by the Federal Power Act. In view of the Supremacy Clause of the Constitution, it is difficult to understand the argument that in case of conflict the State law controls. In this case we are concerned with the validity of a federal order. If that order requires conduct in violation of State law, which we doubt, there would be a direct conflict between federal and state law, and the former would, of course, prevail. If there is no conflict, petitioners' contention based upon Pennsylvania law disappears.

The principle of federal supremacy has been applied to the statutes administered by the Federal Power Commission. *Illinois Natural Gas Co. v. Central Illinois Pub. Serv. Co.*, 314 U. S. 498; *First Iowa Coop. v. Federal Power Commission*, 328 U. S. 152.⁵⁹

Nor can the federal regulation be frustrated by provisions inserted by the state in its corporation law any more than by other forms of state

⁵⁹ In the *First Iowa* case, this Court rejected the contention that Section 9 (b), referred to here by Penn Water (Br. No. 428, p. 71), left in effect the requirements of Iowa law relating to the development of navigable waters which were in conflict with those of Part I of the Federal Power Act.

regulation. In *Northern Securities Co. v. United States*, 193 U. S. 197; where defendants urged that the stock acquisitions, which were claimed to result in an illegal combination under the Sherman Act, were permitted by the law of the state of incorporation and therefore that the Sherman Act as applied to defendants unconstitutionally trespassed upon rights conferred by state law, this Court rejected this contention, saying (193 U. S. at 345-346):

Such a view cannot be maintained without destroying the just authority of the United States. It is inconsistent with all the decisions of this court as to the powers of the National Government over matters committed to it. No State can, by merely creating a corporation, or in any other mode, project its authority into other States, and across the continent, so as to prevent Congress from exerting the power it possesses under the Constitution over interstate and international commerce, or so as to exempt its corporation engaged in interstate commerce from obedience to any rule lawfully established by Congress for such commerce. It cannot be said that any State may give a corporation, created under its laws, authority to restrain interstate or international commerce against the will of the Nation as lawfully expressed by Congress. Every corporation created by a

State is necessarily subject to the supreme law of the land.⁶⁰

Indeed, any other conclusion would virtually destroy any possibility of effective uniform regulation of interstate commerce on a national scale.

Petitioners argue that the Federal Power Act does not "give the Federal Power Commission authority to order or condone contractual arrangements violative of such State law" (Br. No. 428, p. 70); that congressional intent to preclude a State from exercising its traditional power must be clear and manifest (*id.* p. 73), and that here Congress intended the federal regulation to be supplementary to State regulation and not to supersede it. Petitioners rely on the purpose of the statute to fill the gap in State power left by the *Attleboro* case, and upon the provision in Section 201 (a) of the Power Act that—

such federal regulation however, to extend only to those matters which are not subject to regulation by the States.

But neither that provision nor the general purpose of the Act meant that the power of the federal agency to establish reasonable wholesale interstate electric rates was to be subject to State

⁶⁰ See also *Otis & Co. v. Securities and Exchange Commission*, 323 U. S. 624, 638; *Securities and Exchange Commission v. Central-Illinois Corp.*, 338 U. S. 96, 131. *Commonwealth & South, Corp. v. Securities and Exchange Commission*, 134 F. 2d 747, 752-753 (C. A. 3); *Securities and Exchange Commission v. Trans America Corp.*, 163 F. 2d 511, 518 (C. A. 3), certiorari denied, 332 U. S. 847.

control, exercised through State corporation laws or otherwise. Rather, the jurisdictional line drawn was that the Power Commission was to "exercise jurisdiction over matters in interstate and foreign commerce to the extent defined in the Act [e. g., transmission or sale at wholesale in interstate commerce] and local matters would be left to the state regulatory bodies" (*Public Utilities Commission v. United Fuel Gas Co.*, 317 U. S. 456, 467). This Court has already held in regard to the parallel Natural Gas Act, that "as to rates to be effective in the future * * * Congress by that Act * * * preempted the regulatory powers over the transportation and sale of natural gas in interstate commerce" (*Public Utilities Commission v. United Fuel Gas Co.*, 317 U. S. 456, 466), with the Power Commission's jurisdiction being "exclusive". *Id.*, at 467; see also *Illinois Natural Gas Co. v. Central Illinois Public Serv. Co.*, *supra*; *First Iowa Coop. v. Federal Power Commission*, 328 U. S. 152; *Jersey Central Power & Light Co. v. Federal Power Commission*, 319 U. S. 61; *United States v. Appalachian Electric Power Co.*, 311 U. S. 377; *Northwestern Electric Co. v. Federal Power Commission*, 321 U. S. 119.

Certainly, in regulating interstate sales at wholesale, the Federal Power Commission would not be bound by a State corporation law or utility charter providing that a company must earn an 8% return on the reproduction cost new of its prop-

erties. The same principle applies here if it be assumed that the order of the Federal Power Commission, valid under the federal statute, is inconsistent with state law.

C. PENNSYLVANIA LAW DOES NOT PROHIBIT ANYTHING WHICH THE FEDERAL POWER COMMISSION HAS PRESCRIBED

Even if there were merit in petitioners' theories as to the supremacy of State laws *vis-a-vis* the Federal Power Act, it would avail petitioners nothing in this case. This will appear from a brief analysis of the State laws upon which petitioners rely.

None of the laws referred to contain specific provisions dealing with the present problem. The Pennsylvania utility law (Pet. Br. No. 429, App., pp. 47-49) is merely the customary statute providing that rates shall be "just and reasonable", service "adequate, efficient, safe and reasonable", and that utilities may not abandon or surrender services or rights or transfer their property without a certificate of public convenience. The provision of the State corporation law cited (*id.*, pp. 49-50) is the general section to the effect that a corporation shall be managed by its officers and directors.

If, as the Federal Power Commission found, the arrangements here involved were a reasonable means of taking full advantage, both in the public interest and in the corporation's own interest, of the water power of the Susquehanna River,

it is hard to see how a contract so providing could be characterized as an abandonment of the right of managerial control. On the contrary, the contract would seem to be a reasonable exercise of managerial discretion, since Penn Water's resources could not be efficiently developed, without some such arrangement, as its own officers testified (see pp. 16-18, *supra*). Nothing in any of the laws cited would seem to prohibit a board of directors from entering into comprehensive business arrangements, such as the Consolidated contract here involved, which foster the corporate purposes. Cf. *San Diego Water Co. v. San Diego Flume Co.*, 108 Cal. 549; *Venner v. Chicago City Ry. Co.*, 236 Ill. 349; ⁶¹ see, also, *Green Bay R.R.*

⁶¹ In the *San Diego Water* case, the companies entered a contract whereby the Flume Company made the Water Company its sole agent for the sale of water in San Diego, with the combined properties of the companies to be controlled by certain officers as trustees. Subsequently, it was contended that the contract was *ultra vires* because the management of affairs of the corporations was transferred from the directors to the trustees. The California court, however, held that the contract "relates to the sale and distribution of water, and to that extent, at least, it relates to the very purpose of the organization of each of these corporations, and is therefore presumably within their power" (108 Cal. at 558).

The *Venner* case involved a bill to set aside a municipal ordinance accepted by the street railway's Board of Directors on the ground that it involved delegating control to a board of supervisory engineers and was therefore *ultra vires*. The Illinois Supreme Court, however, held that the Board might make any contract that was necessary or proper to enable the corporation to accomplish the purposes of its creation and upheld the contract, including the delegation provision.

Co. v. Union Steamboat Co., 107 U. S. 98, 100; *Hand v. Clearfield Coal Co.*, 143 Pa. 408. Petitioners have cited no Pennsylvania cases to the contrary.⁶²

In any event abandonment of control here could be attributed only to Articles IV and V, which, as we have shown, are not prescribed by the Federal Commission. Insofar as deprivation of initiative with respect to rates and services is concerned, nothing in the Power Commission's order has that effect. Whatever may have been true under the contract prior to the Commission's order, Penn Water undoubtedly retains the right to petition the Commission to modify any of the provisions of its order, including both the provisions specifying the method of payment and Articles IV and V, if they are thought to have been prescribed by the Commission.

It is contended that the assured return provision of the contract and rate order, deprives

⁶² The cases relied on by petitioners (Br. in No. 428, p. 69, first footnote) are not in point. For example, of the two Pennsylvania cases cited, one, *Dubbs v. Kramer*, 302 Pa. 455, involved the invalidity of a contract entered into by a director binding himself to vote a certain way at the directors' meeting. The other, *Severance v. Heyl & Patterson*, 123 Pa. Super. 553, involved the question whether a corporate officer has authority, without express delegation from the Board of Directors, to change a contract entered into by the Board. The other cases typically involved contracts not made by the Board of Directors which attempted to bind in advance the judgment which the Board is supposed to exercise in furthering the interests of the corporation.

Penn Water of incentive to exercise such initiative. The same could be said of any cost-plus contract, and yet such contracts are obviously not *ultra vires* for all corporations, as petitioners' arguments would imply.

Petitioners also refer to common law decisions of this and other courts⁶³ holding that utility companies cannot abandon their obligations under their franchises to competitors, or enter into a division of profits with competitors. None of these cases deals with circumstances such as are presented here, or remotely suggests that a corporation may not comply with the valid order of a regulatory agency prescribing utility rates. And none holds that such an order, when authorized by regulatory statute, would be invalid because of conflict with the common law.

In general, it is fair to say that the cases cited by petitioners reflect the same public policy manifested in the antitrust laws. Accordingly, they do not advance petitioners' position beyond the argument based upon the specific statutes expressing federal antitrust policy.

In short, Pennsylvania law does not prohibit anything which the Federal Power Commission has prescribed, and if it did the federal statute would prevail.

⁶³ Notably, *Gibbs v. Baltimore Gas Co.*, 130 U. S. 396. See Pet. Br. in No. 428, p. 69n.

IV

THE COMMISSION'S ORDERS WERE NOT BASED ON ILLEGAL PROVISIONS OF THE SAFE HARBOR CONTRACT

Petitioners' attack on the Commission's orders under the federal anti-trust laws and under state corporation and public utility laws, involves, as we have indicated, not only the Fourth Circuit's decision, already discussed, invalidating the Penn Water-Consolidated contract, but also the decision invalidating the Safe Harbor contract in the case now pending on petitions for certiorari in Nos. 611, 612.⁶⁴ Thus Penn Water argues that the rate reduction "orders in numerous respects (most notably in connection with the FPC's asserted jurisdiction over Penn Water's Pennsylvania business * * *, determinations of cost of services to and determinations of revenues received from the various customers and the cost allocation under which the major share of the rate reduction is given to Consolidated * * * were predicated upon the fictitious 'entitlements' * * * provided for in the Safe Harbor contract rather than upon actual operations and power actually supplied," that contract having "been adjudged illegal *per se* (Br. No. 428, pp. 67-68; see also pp. 54-58, 68-76, and Br. No. 429, pp. 20, *et seq.*). But, as will readily appear, petitioners' contentions with respect to the *Safe Har-*

⁶⁴ No. 428, Pet., pp. 1, 3, 4, 9, 14, 15, 17, Br., pp. 1-2, 3, 4, 8-10, 11-12, 13-14, 17-18, 19, 67-68, 68-76; No. 529, Pet. pp. 29, 38, Br., pp. 2, 6, 8-9, 10-12, 13, 20-32.

bor antitrust decision are answered by some of the considerations already discussed in connection with the *Penn Water* antitrust case, and the Fourth Circuit's decision in the *Safe Harbor* antitrust case is plainly an insupportable collateral attack on a Commission-prescribed rate order.

A. INsofar AS ENERGY PURCHASED FROM SAFE HARBOR WAS INVOLVED IN FIXING PENN WATER'S RATES, THE COMMISSION'S ORDERS ARE FOUNDED ON THE SERVICES RENDERED BY SAFE HARBOR UNDER ITS PRIOR ORDER FIXING SAFE HARBOR'S RATES.

The Commission, in reducing Safe Harbor's rates to its two owner-customers, Penn Water and Consolidated, on November 4, 1946, prescribed a rate of the same sort as the one it later prescribed in the instant case for Penn Water's sale to Consolidated. The prescribed payment consisted of an annual amount, to be paid by the respective customers in the same $\frac{1}{3}$ - $\frac{2}{3}$ ratio in which Safe Harbor's energy was being sold to them,⁶⁵ the total amount to be com-

⁶⁵ Penn Water's contention that the service being rendered should be determined "on the basis of the power actually delivered to Consolidated" (Br. No. 428, p. 55) would mean that Safe Harbor sells none of its output to Consolidated because it is all physically delivered onto the lines of Penn Water. If Penn Water is to be understood as meaning power which it receives from Safe Harbor and delivers to Consolidated, then its reliance on physical deliveries is no more than an assertion that none of the rest of Safe Harbor's output is received by it for Consolidated's account—an assertion which is without support in the history of the development of the Safe Harbor project and the pool, in the contract terms, or in the physical operations, and is contrary to the

puted by a formula for determining the cost (including cost of invested capital) actually incurred in rendering the services. *Safe Harbor W. P. Corp.*, 5 F. P. C. 221, 266-269, 66 PUR (NS) 212, 255-256.

Except for changes in the provisions of the June 1, 1931, contract, and supplements, relating to the rate of return, the computation of the rate base to which the rate of return was to be applied, and a related change in the computation of the annual depreciation expense allowance, the Commission's order prescribed the June 1, 1931, contract, as supplemented, including the terms which the Fourth Circuit viewed as in restraint of trade.

In compliance with the Commission's order, but expressly reserving "the right to contest the validity of the Commission's order" in the United States Court of Appeals for the Third Circuit, Safe Harbor filed revisions to its Rate Schedule F. P. C. No. 1 (6 F. P. C., at p. 570). The revisions were approved and accepted by the Commission, and the rate schedule previously filed,⁶⁶ as thereby revised, was permitted to be-

order of the Commission fixing the sale to Consolidated as $\frac{2}{3}$ of the total output. Penn Water seeks to deny Consolidated $\frac{2}{3}$ of Safe Harbor's output although Consolidated pays $\frac{2}{3}$ of Safe Harbor's costs of service.

⁶⁶ The Safe Harbor contract of 1931 was first filed informally with the Commission on July 15, 1931, and again filed on December 28, 1932, in response to a letter from Chairman McNinch and the Commission's Order No. 31 requiring li-

come effective as the rate schedule prescribed by the order of November 4, 1946, being designated as Supplement No. 3 to Rate Schedule F. P. C. No. 1. 6 F. P. C. 570-571. The Commission's order was challenged on many grounds in a statu-
censees to file their rate schedules and contracts. It was subsequently filed under Sections 205 (c) and (d) of the Federal Power Act on January 14, 1936.

The contract has been brought before the Commission repeatedly in formal proceedings, as affiliated company profits have been eliminated, interlocking directorates have been broken up, and rates reduced by the Commission, without interfering with the pool operation under that contract. It was incorporated in the record and was discussed in connection with the pool operation in the *Safe Harbor* original cost case in 1935 (1 F. P. C. 230) and in the first *Safe Harbor* rate case (2 F. P. C. 182, 34 PUR (NS) 236, reversed on other grounds, 124 F. 2d 800, certiorari denied, 310 U. S. 663). In the latter case, as in the present case (~~4 F. P. C. 697~~¹⁵⁻¹⁷, *supra*), the testimony of Penn Water's President contrasted the benefits of the *Safe Harbor* contract, embodying a fixed return, with the difficulties inherent in a contract with a unit rate for demand and energy.

The pool operations came before the Commission again when it ended the system of interlocking directors and officers among Penn Water, *Safe Harbor* and Consolidated. *John Edward Aldred, et al.*, 2 F. P. C. 247, 35 PUR (NS) 361.

The contract came before the Commission yet again when, at the request of the Maryland Commission and others, the Commission initiated its investigation in the second *Safe Harbor* rate case (4 F. P. C. 696-697), in which it undertook to determine whether it should "fix by appropriate order or orders, just and reasonable rates, charges * * * practices or contracts" for *Safe Harbor* (4 F. P. C. at p. 697). In the course of the hearing Penn Water's President and Vice President both testified to the difficulties of pricing the output of the *Safe Harbor* project on a unit of service basis and to the virtues of the method finally developed and embodied in the *Safe Harbor* contract.

tory review proceeding in the Third Circuit, and sustained in all respects. *Safe Harbor W. P. Co. v. Federal Power Commission*, 179 F. 2d 179, certiorari denied 339 U. S. 957.

When, therefore, in the Commission's 1949 opinion-order in the Penn. Water rate proceeding which is here under review (on a record closed July 16, 1947, more than seven months after the effective date of the *Safe Harbor* order) the Commission referred to receipts of Safe Harbor energy (R. XVI, 4857-4858), to the Safe Harbor power contract (R. XVI, 4859), and, in its discussion of allocation of costs of service, to "entitlements" to Safe Harbor's output (R. XVI, 4970, 4976, 4978), it necessarily was referring to the energy flows and entitlements under the contract revision prescribed by the Commission as Safe Harbor's rate schedule. For the rate provisions of the contract had by then been superseded by those which had been fixed by the Commission.

That the Commission did rely on its own previously prescribed Safe Harbor rate in fixing Penn Water's rates, is made clear in the Commission's opinion (R. XVI, 4960):

The adjustment of the cost of power purchased from Safe Harbor, an increase of \$37,063, has been made to give effect to the rate order of this Commission in the *Safe Harbor*, case, *supra*. * * *

B. SAFE HARBOR'S RATES DULY PRESCRIBED BY THE COMMISSION ARE NOT TO BE JUDICIALLY INVALIDATED IN A COLLATERAL PROCEEDING

In view of the fact that the Commission relied, as we have just shown, on its own orders in the *Safe Harbor* case and not on the Safe Harbor contract, petitioners' contention that the Commission based its orders herein in part on provisions of a contract declared illegal by the Fourth Circuit amounts in effect to the contention that the Fourth Circuit could invalidate the Commission's rate order in the *Safe Harbor* case, which had previously been upheld on direct review by the Third Circuit.

But the Fourth Circuit obviously has no such power. Under the Power Act orders of the Commission are reviewable only by way of a petition, filed within sixty days of the Commission's order, for direct review in a court of appeals. Sec. 313 (b); *Federal Power Commission v. Pacific F. & L. Co.*, 307 U. S. 156, 159. There can be no direct review in a district court and, even more clearly, no review by way of collateral attack in a proceeding to which the Commission is not even a party. And yet, it is upon such a proceeding, filed in the District Court for Maryland, that petitioners rely for their assertion that the Commission's order in the *Safe Harbor* case has been nullified. The fact that the Commission's order was upheld by the Third Circuit only serves to make this argument more astounding.

As long as the statute contains an adequate procedure for review of the Commission's order, that procedure must be followed, even as against the Commission itself. *Myers v. Bethlehem Shipbuilding Corp.*, 303 U. S. 41. And an order which is not set aside on such a direct review—and even more clearly when its legality has been judicially affirmed—cannot be challenged collaterally and must be accepted by other courts and parties as binding. With respect to rates fixed by the Federal Power Commission, this Court has recently said (*Montana-Dakota Utilities Co. v. Northwestern Pub. Serv. Co.*, 341 U. S. 246, 251):

It can claim no rate as a legal right that is other than the filed rate, whether fixed or merely accepted by the Commission, and not even a court can authorize commerce in the commodity on other terms.

This does not mean that a party may not move the Commission to modify a rate schedule already entered if grounds for such a proceeding appear.⁶⁷

⁶⁷ An application which is in substance only a petition for rehearing must be filed within 30 days. Sec. 313 (a). Moreover, under Sec. 205 (d) of the Act and Part 35 of the Commission's Rules (18 C. F. R. §§ 35.1, et seq.) such a rate could be terminated or changed only by complying with the 30 days' advance notice and the filing requirements of Sections 205 and 206, and would then be subject to complaint and investigation of the new rate under those sections, as well as subject to the right of customer companies or state commissions to seek Commission action with respect to compelling sale or interchange of energy or adequate service under Sections 202 (b) or 207 of the Act (*supra*, pp. 39-42, 77 n.).

The Commission is always open. Such a proceeding before the Commission itself is the only way in which an order already sustained may be attacked.

This principle applies to objections to a Commission order based on antitrust grounds as much as to other objections. Certainly as to private parties that has long been the law. *United States Navigation Co. v. Cunard S. S. Co.*, 284 U. S. 474. *Far Eastern Conference v. United States*, No. 15, Misc. decided March 10, 1952, reaffirms, the principle and even extends it to antitrust proceedings brought by the government. Those cases hold that even where a regulatory agency has not entered an order, resort must first be to the agency when it has jurisdiction over a problem containing both antitrust aspects and calling for the exercise of administrative discretion. *A fortiori*, must there be resort to the statutory procedure when the object is to attack an order of the agency itself.

C. THE COMMISSION'S ORDER IN THE SAFE HARBOR CASE DOES NOT VIOLATE THE ANTITRUST LAWS

As has been pointed out, the Commission's order in the *Safe Harbor* case prescribes the prior contractual arrangement as the new rate schedule. That order was governmental action, not a private

And "until changed in the manner provided" by the Act, the provisions of the rate schedule are "obligatory alike upon carrier and shipper." *Robinson v. B. & O. R. R.*, 222 U. S. 506, 510.

contract or arrangement. For all of the reasons set forth in Point II-A (1) (pp. 49-56, *supra*), the antitrust laws are not applicable either to the order itself or to conduct pursuant thereto to avoid statutory penalties. In addition, the order in the *Safe Harbor* case, like the order in this case, was a *rate* order. Such orders in particular, for reasons stated in Point II-A (2) (pp. 56-63, *supra*), are subject to control by the rate-making agency and not through the antitrust laws. The Fourth Circuit decision in the *Safe Harbor* case seems to contravene both of these established principles, as well as the doctrine of primary jurisdiction.

The Fourth Circuit concluded that the Commission did not prescribe restrictive conditions in the contract as part of its rate order in the *Safe Harbor* case. But this interpretation is contrary to the words of the order itself⁶⁸ as well as to the Commission's interpretation of its own order. What the Fourth Circuit seems to have had in mind was that the Commission's action in attaching the "in and of themselves lawful" clause

⁶⁸ The order provides (5 F. P. C. 221, 269), "The Commission orders that: * * * (B) Safe Harbor shall file revised rate schedule F. P. C. 1, dated June 1, 1931, and supplements thereto, providing for a 5 percent return on a rate base computed in accordance with findings (12) to (17) above, inclusive, said revised schedule to be effective on and after January 1, 1947 * * *." "F. P. C. 1" was the *Safe Harbor* contract.

The subsequent paragraphs of the order detail the method whereby *Safe Harbor* was to compute its rate base.

to the order in the instant case shows that it would not have approved the conditions found to be unlawful by the Fourth Circuit in the *Safe Harbor* antitrust case if the antitrust contention had been presented to it. We do not know whether this assumption is valid, and whether the Commission, had the issue been raised, would have attached similar conditions in the *Safe Harbor* proceeding. The questioned portions of the *Safe Harbor* contract do not seem to have the same effect as those in the *Penn Water* case, as the petitions for certiorari in Nos. 611 and 612 point out. The Commission might also reasonably have concluded that the allegedly restrictive conditions were separable from the remainder of the contract, as the petitions for certiorari vigorously, and it seems to us reasonably, contend. If so, the Commission might have prescribed all of the contract except those conditions, or some of them, instead of throwing out the entire arrangement as did the Fourth Circuit. All of these possibilities demonstrate the wisdom, indeed the legal necessity, of requiring application to the Commission for a construction or modification of its own order instead of permitting collateral attack on a ground not raised before the Commission in a private suit to which the Commission is not even a party.

For the above reasons we do not think it necessary, or even proper, for this Court to determine for itself the validity under the antitrust

laws, or otherwise, of the particular contract provisions held unlawful by the Fourth Circuit in the *Safe Harbor* case. For the Commission itself, which has made the provisions a part of its order, is the agency to which the matter should be submitted—if the matter is not already foreclosed by the prior review proceeding in the Third Circuit. It should be noted, however, that there is an important difference between the provisions requiring one company's consent to the other's action when a part of a Commission order and not merely a private contract. For consent provisions in filed rates do not restrain the interested parties from filing an amendment to a rate schedule at any time, or from asking the Commission to amend a rate schedule, even one to eliminate the consent requirement itself. To illustrate: If any party is dissatisfied with having to obtain a consent now required by the Commission's rate order, it may file a proposed rate schedule or complaint seeking elimination of the consent requirement. The proposed change will be considered by the Commission on the basis of the current relevant facts, and acted on in the light of the governing legal principles, subject to judicial review under Section 313 (b) of the Act. A "restrictive provision" in a filed rate has thus an entirely different effect from a similar provision in an agreement not subject to statutory filing requirements and Commission regulation. A filed rate is subject to Commission alteration

in the public interest. An unregulated agreement restraining the parties from economic activity in which they would otherwise be free to engage, may be unalterable unless declared illegal by the courts under the antitrust laws.

For all of the above reasons we submit that the Safe Harbor order of the Commission was, and must be accepted as, binding and in force, and that it was entirely correct for the Commission so to assume in coming to its decision in the instant case. This leads to the conclusion that there is no basis for petitioners' contention that the order in this case should be set aside because of the "invalidity" of the Safe Harbor order. Also, it leads to the conclusion that the Fourth Circuit decision in the *Safe Harbor* antitrust case, now before this Court on petitions for certiorari in Nos. 611 and 612, was clearly erroneous.

V

PENN WATER'S SALES FOR RESALE TO ITS PENNSYLVANIA ELECTRIC UTILITY CUSTOMERS ARE IN INTERSTATE COMMERCE

The Pennsylvania Commission (but not Penn Water) contends that Penn Water's sales to its Pennsylvania electric utility customers are not in interstate commerce and hence that, although these sales are for resale, they are beyond the jurisdiction of the Power Commission to regulate. Even if it were assumed that this contention were well founded, it would not affect the rate reduction ordered in Penn Water's rates to Consoli-

dated in Maryland, which appear in a separately prescribed tariff which applies only to the interstate transmission of electric energy.⁶⁹

In any event, the sales regulated by the Power Commission were all in interstate commerce, as both the court below in this case and the Court of Appeals for the Third Circuit in the *Safe Harbor* cases have held.⁷⁰

⁶⁹ The Pennsylvania Commission would not seem to be in a position to complain of this (if it is correct in its contention that the Federal Power Commission's authority does not extend to the Pennsylvania sales), even though it believes that a greater share of the reduction should be assigned to Pennsylvania. Although the Pennsylvania Commission's brief indicates dissatisfaction with the allocation (pp. 32-42), neither petitioner has brought that question here. Each refers to the allocation only as showing that the Power Commission relied on the private contract in determining the new rates.

⁷⁰ In its second *Safe Harbor* opinion (*Safe Harbor W. P. Co. v. F. P. C.*, 179 F. 2d 179, 184-185, certiorari denied, 339 U. S. 957, the Third Circuit stated as to *Safe Harbor's* sales:

"As we pointed out in our earlier opinion, 124 F. 2d at page 802, *Safe Harbor's* output is delivered to an integrated interstate electric system under the terms of the so-called '1931 contract,' two-thirds of the energy being sold to the Maryland Company and the remaining one-third going to the Pennsylvania Company. The Commission has correctly stated, 'The sales are sales for resale,' 5 F. P. C. at p. 235. They constitute in fact wholesale sales in interstate commerce."

Safe Harbor's energy moved into commerce through Penn Water's transmission lines and pursuant to precisely the same arrangement as power generated at Penn Water's own project.

The Federal Power Commission is authorized to regulate "the sale of electric energy at wholesale in interstate commerce." Section 201 (b). As we have seen (pp. 11-15), the pooling of hydro and steam power necessitated by the variable flow of the Susquehanna has resulted in the operation of the hydro and steam plants of Penn Water and Consolidated as an integrated system, and of the sale of their product as a single unit. When the river flow is high, the power runs from Penn Water's plant in Pennsylvania to Baltimore and to the Pennsylvania customers. In other parts of the year, power is transmitted from Penn Water's plant during the peak periods of the day or week, but from Baltimore the remainder of the time, during which the river water is impounded and reserved for the peak periods. The amount which will move to the Pennsylvania customers from either the Baltimore or Pennsylvania plants on any particular day must be determined, day by day, as affected by the flow of the river. It is true that after the event the approximate amount of power transmitted to all of Penn Water's Pennsylvania customers from each source can be determined, and that on an annual basis in 1946 83% of the energy used by those customers was generated in Pennsylvania.⁷¹ This

⁷¹ The 83% is nothing more than the relationship of Pennsylvania-generated energy to total energy from both states in 1946. It does not represent the percentage of Pennsylvania energy involved in the sales to any individual Penn Water customer. Such data are not available from meter

figure reflects the fact that in months of high river flow none of the power used in Pennsylvania is obtained from Consolidated's steam plants in Baltimore. But in certain parts of the day or week during the long low water periods, all or most of the power used in Pennsylvania comes from the Baltimore plants. And at some times both Maryland and Pennsylvania power will be mingled in the transmission lines.

By careful coordination which supplies power from the most economical source irrespective of

readings, for the meters registering the amount of energy sold to the Pennsylvania customers do not identify the source of the energy involved in the sales. It is doubtful whether metering could be developed which would provide such data. To secure such data of that nature as are contained in the Record required elaborate engineering studies of the movement of electric energy on the integrated system, based on reasonable assumptions with respect to the behaviour of electric energy flows. The nature of the complex hourly computations which would be required to identify the percentages of out-of-state energy involved in the sales to the Pennsylvania customers if, for purposes of regulation and billing, segregations between out-of-State and in-State energy were necessary, is illustrated by the studies of flows of electric energy made by staff engineers for 20 days of the year 1944 (Tr. LVIII, 22350-22370) and 30 days of the year 1946 (R. XIV, 4405-4435). Those studies involved elaborate calculations consuming many months (RI. 351-375; RV. 2279-2285). They were made for the purpose of establishing the approximate magnitude of out-of-State energy involved in the sales to the Pennsylvania customers under certain river conditions. Such studies showed that individual Pennsylvania utility customers received 100% Maryland generated energy for substantial periods of time and lesser percentages for longer periods of time (RI. 362, 370, 371, 374, 375; RV. 2282-85).

State lines, the integrated system has been able to supply a much larger utility load than would result from the mere addition of the capacities of the several plants if operated independently, and has been able to do so at much less than the average of the costs of such independent operation.

The sale which the Power Commission was regulating was the sale of the product of this integrated interstate system, some generated in Maryland and some in Pennsylvania. The Pennsylvania customers who obtained the firm power necessary for such communities (as York, Lancaster and Coatesville) would not have purchased the power generated by Penn Water alone at its Pennsylvania facilities. If they had, the cities would have been without power, or without enough power, many times during the year. The product sold, consisting of energy and capacity assuring reliable year-around service to the Pennsylvania communities, is not a mere composite of the products of the individual plants but an interstate product whose nature and very existence are wholly dependent on the continued operation of the integrated interstate system. The product Penn Water sells to the Pennsylvania customers is a product whose availability and low cost has been made possible by the interstate pool which places Penn Water in a position to draw upon Consolidated's out-of-

state steam generators when needed. As the court below held (R. XVIII, 5384):

* * * Because such an energy pool, drawing upon the extensive steam and hydro capacities of Penn Water, Safe Harbor and Baltimore Company now exists, both Penn Water and Baltimore Company have been able to satisfy commitments which would otherwise be outside their individual capacities, as they are now constituted. Given such interconnected and integrated interstate wholesale operations, there can be no such thing as assigning a particular sale solely to operations within Pennsylvania. Each sale is in effect a pool sale drawn from the integrated interstate system and hence interstate in nature.

The sales here regulated by the Power Commission are thus interstate sales. They included an inseparable and essential quantity of power crossing the State line. The fact that some intrastate energy is also included does not make the sale an intrastate one.

Interstate commerce, both generally and as reflected in the Federal Power Act, is not an artificial or abstract or "technical legal conception, but a practical one, drawn from the course of business" *Swift and Company v. United States*, 196 U. S. 375, 398. Here we are concerned with a law designed to regulate interstate rates. If some of the energy sold as a part of a

single, inseparable transaction is interstate, it is obvious that the entire sale must be treated as interstate for purposes of rate regulation. No company could operate under a system whereby a state commission would fix the rates for the energy sold in the spring months of high water and in other parts of the year from 4:00 to 7:00 p. m. on week days, and a federal commission the remainder of the time. And here the problem is not nearly that simple, inasmuch as the periods and the quantity of power coming from one source or the other vary from day to day and from hour to hour.

Since the source of the power used depends ultimately upon the quantity of rainfall in the Susquehanna watershed, it can only very roughly be estimated in advance whose energy will be used. Rates, however, must be determined in advance, for a period of some duration in the future. They cannot be fixed after the fact, when it has been determined that a certain percentage during the preceding year—or week—came from one source rather than the other.

It is thus obvious that the rates for a single interstate transaction of sale must be prescribed by a single agency. Since the arrangement whereby the river flow is used most economically requires a unitary operation including sales to Maryland and to and within Pennsylvania, that agency cannot as a practical matter be the organ of a single state. Furthermore, when the Power

Act was passed in 1935, the states lacked constitutional power over interstate wholesale rates and thus could not have regulated the interstate portion of the integrated enterprise.

The purpose of Congress was to fill the gap in which the states could not act. The Power Commission's authority to regulate rates for interstate sales thus undoubtedly was intended to cover this type of inseparable interstate and intrastate operation. As this Court said in dealing with a similar statutory problem in *United States v. New York Central R. Co.*, 272 U. S. 457, 464:

Where, as here, interstate and intrastate transactions are interwoven, the regulation of the latter is so incidental to and inseparable from the regulation of the former as properly to be deemed included in the authority over interstate commerce conferred by statute. * * * An interpretation of the statute which would in practice require the segregation of all shipments in interstate commerce would make compliance with the commission's orders impossible and defeat the purpose of the Act.

The considerations underlying the familiar cases of interstate and intrastate commingling in the constitutional field (*e. g.*, *Southern Railway Co. v. United States*, 222 U. S. 20; *Colorado v. United States*, 271 U. S. 153, 164; *Currin v. Wallace*, 306 U. S. 1) also provide a helpful analogy.

Missouri v. Kansas Gas Co., 265 U. S. 298, and

Public Utilities Commission v. Landon, 249 U. S. 236, support this conclusion. In both cases, Kansas Natural Gas Company transported gas from Oklahoma into Kansas, mingled it with gas produced in Kansas, and sold it for resale to local distributing companies in both Kansas and Missouri. At the time of the *Landon* case, 6% of the gas sold in Kansas was produced in Kansas (249 U. S. at p. 242), while at the time of the *Missouri* case the Kansas gas comprised 34% of the mixture.⁷² It was assumed without question that this did not affect the interstate nature of the wholesale sales of the entire system, including the sales in Kansas made partially from Kansas gas.

The same problem was considered explicitly in *Kentucky Natural Gas Corp. v. Public Service Commission*, 28 F. Supp. 509 (E. D. Ky.), affirmed, 119 F. 2d 417 (C. A. 6), the facts of which are closely analogous to those of the present case. In the *Kentucky Natural Gas* case, the company owned and operated a pipe line system located partly in Kentucky and partly in Indiana. Some of the gas transported in the system was obtained in the State of Kentucky and mixed with some obtained in Indiana. The mixed gas moved from one state to the other depending upon the needs of the system, and was

⁷² *Kansas Gas Co. v. Kansas*, 265 U. S. 298, No. 133, Oct. Term, 1923, Tr. of R., p. 13.

used by Kentucky Natural in making wholesale sales to local distributing companies at points in both states. At times, Kentucky Natural obtained about half of the gas sold in Kentucky from that state, but this proportion varied greatly from time to time. The Kentucky Commission sought to regulate the company's sales in Kentucky, but the court of appeals held that appellee "is engaged solely in interstate commerce," and that exclusive jurisdiction had been conferred on the Federal Power Commission under the Natural Gas Act.⁷³

Peoples Gas Co. v. Public Service Commission, 270 U. S. 550, and *Lone Star Gas Company v.*

⁷³ The opinion of the district court, which the court of appeals adopted, had stated (28 F. Supp. at 512, 513):

"The record shows that the business of the complainant is a closely integrated transportation system which is fundamentally and predominantly interstate in character from beginning to end. In structure and operation, such continuity exists throughout the system that regulation at one point or control of a single activity would necessarily affect the whole structure. The sale and delivery of gas at wholesale from the interstate pipe line to local distributing companies is an integral part of the major enterprise, commerce between the states. Under such circumstances, regulation in the public interest is national rather than local, demanding a standard of uniformity unattainable except through a single paramount authority. * * *

* * * * *

"The established course of business being predominantly interstate, the mere fact that some gas from the interstate stream is sold and delivered in the state of its origin affords that state no superior power to regulate or control the transaction."

Texas, 304 U. S. 224, relied upon by the Pennsylvania Commission do not conflict with the conclusion that all Penn Water sales are interstate. In the *Peoples Gas* case, the Court held that Pennsylvania could require ~~the~~ company to supply the needs of the City of Johnstown, Pennsylvania, with Pennsylvania gas commingled in a pipeline with West Virginia gas but in known quantities sufficient for that purpose. The Court ruled that the Pennsylvania gas, even though physically commingled, was separable from the West Virginia gas and was in intrastate commerce. Here we have no such relatively simple and stable situation. The demands of the Pennsylvania customers of Penn Water cannot be supplied from sources within Pennsylvania for substantial periods of the year. When water is being impounded, most of their power comes directly from Maryland. The constantly shifting demands of the power pool for Maryland and Pennsylvania power in varying quantities makes it impossible for purposes of rate regulation to separate the power which is both generated and consumed in Pennsylvania. It is also to be noted that at the time of the *Peoples Gas* case, there was no federal regulation, and that the alternative to control by Pennsylvania was no regulation at all. In every significant respect, therefore, the *Peoples Gas* case is distinguishable.

The *Lone Star* case is even less in point. The Court there held that for the ultimate purpose

of regulating retail rates charged by local distributing companies; Texas could determine the reasonable charge for gas delivered by affiliates to the distributing companies, even though some of the gas came from Oklahoma. Since the rate to be paid by one affiliate to another is primarily a bookkeeping transaction the substance of the case was Texas' right to determine costs as a basis for fixing the retail rates for the subsidiaries. Cf. *Western Distributing Co. v. Public Service Commission*, 285 U. S. 119, 124; *Dayton Power & Light Co. v. Public Utilities Commission*, 292 U. S. 290, 295; *American Telephone & Telegraph Co. v. United States*, 299 U. S. 232, 239. In view of these circumstances; which of course differ materially from those at bar, the Court found that Texas was not regulating sales and deliveries in interstate commerce. 304 U. S. 236-237. The Court did not hold that a sale of an interstate and intrastate product as a unit would in other circumstances or generally not be an interstate sale.

It follows, therefore, that the Commission has jurisdiction over these sales by virtue of the Federal Power Act. The Pennsylvania Commission's claim that these sales are nevertheless matters of local concern is meaningless in this case. Not only has this Court held to the contrary by ruling that sales for resale in interstate commerce are of national concern beyond the power of the states to regulate (*Public Utilities Commission v. Attle-*

boro Steam & Electric Co., 273 U. S. 83, 90), but Congress has occupied the field by vesting control over sales for resale in interstate commerce in the Power Commission. Cf. *Illinois Gas Co. v. Public Service Co.*, 314 U. S. 498, 506.

VI

THE CONTENTION THAT A LICENSEE SUBJECT TO REGULATION UNDER PART I OF THE POWER ACT MAY NOT ALSO BE REGULATED UNDER PART II IS IRRELEVANT HERE, SINCE PENN WATER'S RATES WERE FIXED UNDER BOTH PARTS, AND, IN ANY EVENT, IS UNSOUND

Penn Water argues that it may not be regulated under Part II of the Power Act because it is a licensee subject to regulation under Part I. Inasmuch as the Commission's order in this case was based upon Part I and Part II, it is difficult to see what difference this would make, even if true, so far as this case is concerned. Neither of petitioners is asserting that any of the jurisdictional or other requisites necessary to make the order valid under Part I are absent (apart from Pennsylvania's contention as to interstate commerce considered in the preceding point).

Part I of the Federal Power Act applies to licensees authorized to construct hydroelectric projects in navigable streams or on public lands. Section 20 provides that when the "power or any" part thereof shall enter into interstate or foreign commerce," the rates charged and the service furnished by the licensee "shall be reasonable, nondiscriminatory, and just"; and that when the

states concerned are unable to agree, the Power Commission may enforce the section with respect to rates and services which constitute interstate commerce.

The Commission's finding that the states of Maryland and Pennsylvania are unable to agree is not, and cannot well be, challenged in this case.⁷⁴ And the standard of rate regulation—reasonable, nondiscriminatory and just—is precisely the same as that contained in Part II. Sections 205 and 206.⁷⁵

As we read Penn Water's brief, which is, of course, addressed to the opinion below, the prime relevance of the argument as to Parts I and II is that if the Commission can act only under Part I it is bound by the antitrust provision in Section 10 (h) of that Part. This, it is said, would invalidate the argument advanced by the court below (but not by the Government here) that Section 10 (h) is inapplicable here because repealed by Part II insofar as licensees subject to that Part are concerned.

We have shown in Point II B (*supra*, pp. 63–65) that Section 10 (h), like the Sherman Act, applies only to private business combinations, not to conduct ordered by the Government and that, accordingly, assuming its applicability to licensees

⁷⁴ See the contrary positions taken in their briefs filed in this Court.

⁷⁵ We discuss below (pp. 129–135) Penn Water's argument that a different rate base is required under Part I.

regulable under both Parts I and II, it does not advance Penn Water's position in this case. Although Penn Water's brief attempts to point out other differences between Parts I and II, at no point does it raise any question (other than with respect to Section 10 (h)) as to the possible irregularity of the Commission's order if viewed solely as authorized by Part I. In these circumstances, we think the question as to whether companies subject to Part I are also subject to Part II is academic insofar as this case is concerned.

Although further discussion of the point may be unnecessary, we do not wish to leave Penn Water's argument unanswered, for it is basically unsound. We point out preliminarily that the precise contention advanced here was discussed at length and rejected in the very thorough and well-reasoned opinion of Judge Biggs of the Third Circuit in the *Safe Harbor* case. 179 F. 2d 179, 182-189, certiorari denied, 339 U. S. 957. That court not only held that a licensee may be subject to both Parts I and II, but also that a rate order based upon both parts was valid under both.

A. LICENSEES WHICH QUALIFY AS "PUBLIC UTILITIES" ARE SUBJECT TO REGULATION UNDER PART II AS WELL AS UNDER PART I

The basic fallacy in Penn Water's position is its failure to recognize that a company may be both a licensee under Part I and a public utility under Part II and as such be subject to regulation under both Parts. The qualifications for a licensee under Part I, the ownership, operation or

maintenance of a power project on public lands or on or affecting navigable streams, are quite independent of those for a public utility under Part II, the transmission or sale at wholesale of electric energy in interstate commerce. For this reason, many electric companies that are "public utilities" under Part II are not "licensees" under Part I, and conversely many Part I "licensees" do not come within Part II's definition of "public utility."

But where a company transmits or sells at wholesale in interstate commerce electric energy which it has generated at a licensed project, it satisfies the requirements for both a licensee and a public utility, and the fact of the coincidence does not operate to exempt such a company from regulation under Part II, or for that matter, from under Part I. Although the Parts deal with different problems, and contain different provisions,⁷⁶ they are not inconsistent. There thus is no reason why a company which satisfies the definition of a "public utility" as well as a

⁷⁶ Part II provides several kinds of regulation with respect to public utilities which Part I does not provide for licensees: compulsory interconnection on application of another electric company or a state commission (Section 202 (b)); compulsory interconnection or operation in war or emergencies (Section 202 (c)); Commission regulation of sale, lease, and merger or consolidation of facilities, or acquisition of securities of another public utility (Section 203); and Commission regulation of assumption of liability (Section 204). Part III provides, with respect to "public utilities" only, a prohibition of insiders' profits and the pay-

"licensee" should not be subject to regulation under each part simultaneously.

Far from precluding regulation of a company as both a licensee and a public utility, the pertinent language of the Power Act appears to contemplate such dual regulation. Section 201 (e) provides that—

The term "public utility" means *any* person who owns or operates facilities subject to the jurisdiction of the Commission under this Part. [*Italics supplied.*]

The only exemption from this sweeping language appears in Section 201 (f), which excepts governments and their instrumentalities. As the court below pointed out (R. XVIII, 5379):

That section conspicuously makes no reference to Part I licensees. It seems unlikely that Congress would not have included so important a group as federal water-power licensees among the specific exceptions to Part II if it had actually intended to except them.

To read a new exception for a large and well-known class of utilities into the Act would not

ment of dividends from capital (Section 305 (a)); and Commission regulation of interlocking managements (Section 305 (b)).

Likewise, Part I, in addition to regulation pertaining to the licensed project itself, provides some regulation which has no counterpart in Part II, such as Commission regulation of intrastate rates in certain instances, including customers' rates (Section 19), and interstate retail rates in some instances (Section 20).

only be contrary to the words Congress employed but also to the legislative history of Part II, which plainly reveals that Congress recognized that its definition of public utility embraced some licensees and that it intended such licensees to be regulated as public utilities as well. The House Committee on Interstate and Foreign Commerce dealt with this specific matter in recommending amendments to the prohibition in Section 305 (a) against personal profit by company officials. As Section 305 (a) passed the Senate, its prohibition was directed at officials of licensees and public utilities. S. 1725, 74th Cong., 1st Sess. The House Committee recommended that "licensee" be deleted from the Section and that its prohibition be directed solely against public utilities, because it understood that licensees owning or operating Part II jurisdictional facilities would be regulated as public utilities. The Committee commented:

The Senate bill includes *licensees* within the provisions of this section, but inasmuch as *such licensees when interstate operating public-utility companies will be subject to the provisions of the section in any event, licensees have been omitted from the bill as reported, because of the lack of public interest in those companies which are not public utilities.* [Italics supplied.] "

" H. Rep. No. 1318, 74th Cong., 1st sess., p. 31. The conference report on the bill and the Act as passed incorporated the House Committee's changes. H. Rep. No. 1903, 74th Cong., 1st sess., pp. 56, 75; Section 305 (a).

This definite statement by the Committee that licensees will be subject to regulation when "interstate operating public-utility companies" is flatly inconsistent with Penn Water's contention.

Dozier A. DeVane, the Solicitor of the Federal Power Commission and one of the draftsmen of Part II evidenced the same understanding. He stated at the hearings on the proposed legislation that "title II (Parts II and III of the Act) deals with operating companies" and that "among the operating companies are those companies that now have licenses from the Federal Power Commission under the Federal Water Power Act." Hearings before the Senate Committee on Interstate Commerce, 74th Cong., 1st sess., on S. 1725, pp. 233-234.⁷⁸

In contrast to the remarks just referred to, the excerpts from the Committee Report and Hearings quoted in Penn Water's brief (pp. 86-89) do not express any view with respect to whether

⁷⁸ Mr. DeVane's statement occurred in his explanation of why there were proposals at that time to amend the Federal Water Power Act of 1920 (which as amended in 1935 became Part I of the Federal Power Act) and why these proposed amendments were contained in Title II of the Public Utility Act of 1935 (Title I being what is now the Public Utility Holding Company Act of 1935). Referring to what is now Part II of the Federal Power Act as a "second Title II" (although Part II and the amendments of the 1920 Act were included in a single Title II), he said that it was appropriate to amend the old law dealing with licensees at the same time that new legislation (*i. e.*, Part II) was enacted which affected operating companies, including licensees.

licensees are also subject to Part II. Some of them merely assert in various ways that Part II was meant to fill the gap left by the *Attleboro* case, not to encroach upon matters subject to state regulation. The statement of Commissioner Seavey that Title III contains the provisions applicable both to licensees and interstate operating companies can be accorded full meaning in relation to those companies which are only one or the other. It does not imply—and certainly does not say—that a single company, which is both a licensee and an interstate utility, cannot be regulated under both Parts.

B. SECTIONS 20 AND 201 DO NOT LEAVE THE REGULATION OF A LICENSEE'S INTERSTATE WHOLESALE RATES TO THE STATES

Penn Water contends, however, that Section 20 itself authorizes the states, at least when acting jointly, to regulate the interstate rates of licensees, that Section 201 (a) provides that the federal authority under Part II may "extend only to those matters which are not subject to regulation by the States," and that therefore Part II does not permit regulation of the interstate rates of licensees.

Penn Water is incorrect in the meaning it ascribes to both Section 20 and Section 201 (a). As the Court knows, at the time Title II of the Act was passed the states possessed constitutional power, under this Court's decisions, to regulate only retail interstate electric and gas rates; but

not wholesale rates,⁷⁹ and Title II of the Federal Power Act was passed in order to fill this gap. See H. Rep. No. 1318, 74th Cong., 1st Sess., pp. 7-8; S. Rep. No. 621, 74th Cong., 1st Sess., pp. 17, 48; *Federal Power Commission v. East Ohio Gas Co.*, 338 U. S. 464, 472; *Connecticut Light & Power Co. v. Federal Power Commission*, 324 U. S. 515, 525-527; *Jersey Central Power & Light Co. v. Federal Power Commission*, 219 U. S. 61. Since the gap thus revealed did not, however, affect the recognized power of the states to regulate interstate retail transactions (e. g., *Pennsylvania Gas Co. v. Public Serv. Comm.*, 252 U. S. 23), Section 201's exclusion of matters "subject to regulation by the states" from its grant of jurisdiction was aimed at exempting state regulation in the retail area, in which single states had power to act. There is no suggestion in any of the history of the Act of 1935 that the matters subject to state regulation included the interstate wholesale rates of licensees under Section 20. There was no thought, so far as appears, that the gap to be filled by the proposed legislation was anything less than the full scope of the constitutional impotence of the States, or that the gap had already been partially filled by Congress' previous enactment of Section 20.

⁷⁹ *Public Utilities Comm'n. v. Landon*, 249 U. S. 236, 243; *Missouri v. Kansas Gas Co.*, 265 U. S. 298, 310; *Public Utilities Comm'n. v. Attleboro Co.*, 273 U. S. 83, 89; *East Ohio Gas Co. v. Tax Comm'n.*, 282 U. S. 465, 470-472.

Congress had good reason for not suspecting that Section 20 contained a grant to the States of power which was otherwise forbidden by the Constitution. For Section 20 itself contains no affirmative grant of power to the States. The language relating to state regulation is contained in a condition upon the exercise of federal authority. The pertinent portion of Section 20 provides merely—

whenever any of the States directly concerned has not provided a commission or other authority to enforce the requirements of this section within such State * * * or such States are unable to agree through their properly constituted authorities on the services to be rendered or on the rates or charges of payment therefor, * * * jurisdiction is hereby conferred upon the [Federal] commission * * * to regulate and control so much of the services rendered, and of the rates and charges of payment therefor as constitute interstate or foreign commerce * * *.

The absence of any grant of power to the states is to be contrasted with the immediately following grant of regulatory authority to the Federal Commission.

When Congress has intended to permit states to regulate interstate transactions from which they would otherwise be barred it has spoken

much more explicitly.⁸⁰ Congress has also been much more specific when exercising its power to approve interstate compacts.⁸¹

It seems clear that under Section 20 Congress was merely leaving with the States whatever power they possessed to regulate interstate transactions—either individually or in combination—apart from the Federal Power Act. Various statements made in the course of the legislative debate so indicated.⁸² There is no suggestion of an intention to expand such power.

It is probably true that in 1920, immediately after *Pennsylvania Gas Co. v. Public Service Commission*, 252 U. S. 23, and *Public Utilities Commission v. Landon*, 249 U. S. 236, and before the *Kansas Gas*⁸³ and *Attleboro*⁸⁴ cases in 1924 and 1927, the sponsors of the Act believed that the power of the States was not limited to interstate retail rates. But that assumption is not suf-

⁸⁰ In this connection, see *In re Rahrer*, 140 U. S. 545, 549, 562; *Clark Distilling Co. v. Western Maryland Ry. Co.*, 242 U. S. 311, 321, 332; *Whitfield v. Ohio*, 297 U. S. 431, 434, 440; *Kentucky Whip & Collar Co. v. I. C. R. Co.*, 299 U. S. 334, 343, 351; *Prudential Life Insurance Co. v. Benjamin*, 328 U. S. 408, 429-431.

⁸¹ See, e. g., *Olin v. Kitzmiller*, 259 U. S. 260, 262; *Arizona v. California*, 283 U. S. 423, 449; cf. *United States v. Arizona*, 295 U. S. 174, 183; see also Section 11, Natural Gas Act, 42 Stat. 821, 827, 15 U. S. C. 717, 717j.

⁸² Hearings, House Committee on Water Power, 65th Cong., 2d Sess., pp. 66, 99, 101; 58 Cong. Rec. 2239; 59 id. 6537.

⁸³ *Missouri v. Kansas Gas Co.*, 265 U. S. 298 (1924).

⁸⁴ *Public Utilities Commission v. Attleboro Steam and Electric Co.*, 273 U. S. 83 (1927).

ficient to convert the condition imposed upon action by the Federal Commission into an enlargement of State authority. And in 1935, when Congress in reconsidering the entire subject, made the 1920 Act as amended Part I of the new Federal Power Act, it clearly understood that the States could not regulate interstate wholesale rates.

As we have seen, it seemingly occurred to no one in 1935 that Congress had conferred any affirmative power upon the States to regulate interstate wholesale rates when it enacted Section 20 in 1920. Likewise, no indication appears that Congress deemed the States to have had any previously existing power over any interstate wholesale rate or that it intended thereby to vest such authority in the States. Although it had the opportunity to do so in the course of its extensive revision of Part I in 1935, Congress made no change in Section 20 nor indicated any intention of extending Section 20 to permit either individual or joint state regulation of wholesale rates. On the contrary, the legislative history of the 1935 Act is replete with showings that a primary purpose of Part II was to confer jurisdiction upon the Power Commission over all interstate wholesale rates which the *Attleboro* case has "placed * * * entirely beyond the reach of the States" (S. Rep. No. 621, 74th Cong., 1st Sess., p. 17).

For the above reasons Sections 20 and 201, whether read jointly or separately, do not grant

the States authority over the interstate wholesale rates of licensee. There can therefore be no doubt that such power is vested in the Federal Commission by Section 201 of Part II, and that the Commission may fix rates for interstate wholesale licensees under that Part.

C. PARTS I AND II DO NOT IMPOSE INCONSISTENT METHODS OF COMPUTING THE RATE BASE

Penn Water also contends that a licensee's rates cannot be prescribed under both Parts I and II because they impose inconsistent methods of computing the rate base. There is no such inconsistency. On the contrary, the statutory provisions are virtually identical. The rate standard prescribed in Section 20 provides:

* * * the rates charged and the service rendered * * * shall be *reasonable, nondiscriminatory, and just* to the customer and all *unreasonable discriminatory and unjust* rates or services are hereby prohibited and declared to be unlawful * * *
[Italics supplied.]

Section 206 (a), which, together with Section 205 constitutes the rate fixing provisions of Part II, provides:

Whenever the Commission * * * shall find that any rate, charge, * * * is *unjust, unreasonable, unduly discriminatory* or preferential, the Commission shall determine the *just and reasonable* rate, charge * * *. [Italics supplied.]

Thus, in almost identical words, both Parts prescribe the customary standard: "reasonable, nondiscriminatory and just," the very standard which this Court has construed to free regulatory commissions from adherence to any particular formula. *Federal Power Commission v. Hope Natural Gas Co.*, 320 U. S. 591. The rate standards of both Parts, therefore, clearly permit the use of the same formula for determining the rate base.

The basis of petitioners' claim is Section 20's incorporation by reference of the formula for recapture contained in Section 14. The latter Section refers to "net investment" which is defined in Section 3 (13),⁸⁵ and which Penn Water construes as meaning "an undepreciated rate base except where depreciation and other reserves

⁸⁵ The claim for "net investment" as the Section 20 formula for rate regulation is arrived at *via* the limitation on the rate base in that Section to an amount not "*in excess of the value or values prescribed in Section 14 hereof for the purposes of purchase by the United States, * * **" Section 14 (dealing with "recapture" by the United States upon expiration of the license) provides that before taking possession, the United States "shall pay the net investment of the licensee in the project or projects taken, not to exceed the fair value of the property taken * * *."

In so far as here pertinent, Section 3 (13) defines "net investment" to mean "the actual legitimate original cost thereof * * * minus the sum of the following items properly allocated thereto, if and to the extent that such items have been accumulated during the period of the license, from earnings in excess of a fair return on such investment: * * * (b) aggregate credit balances of current depreciation accounts, * * *"

are accumulated from earnings in excess of a fair return" (Br. No. 428, pp. 79-80).

It is not necessary for purposes of this case to delve into the intricacies of the meaning of net investment or the depreciation clause in Section 3 (13). For Section 20 does not refer to the "net investment" provision of Section 14 as the rate base to be used, but as a maximum not to be exceeded. The critical clause provides that "no value shall be * * * allowed by the commission * * * *in excess of the value* * * * prescribed in Section 14." Thus, under Section 20, whatever rate base is used cannot exceed net investment. The sole difference as to rate base between the two Parts, therefore, is that Part I restricts the rate base to one not in excess of net investment.

This difference obviously does not prevent the Commission from prescribing rates under the two Parts simultaneously and with entire consistency. A problem could arise only if the Commission sought to apply a formula which would produce a rate base under Part II *higher* than that permissible under Part I. The petitioner is not asserting that the formula which the Commission employed here was too high.

As a matter of fact since its first annual report after the passage of the 1920 Act, the Commission has interpreted the Section 3 (13) formula as identical with the tests it now employs under

Part II. First Annual Report to Congress (1921), (H. Doc. 242, 67th Cong., 2d Sess., p. 57).

Moreover, even if net investment as defined in Section 3 (13) were considered as a formula for rate regulation under Part I, there would be no conflict of rate formulas. Under both the net investment formula and that used by the Commission under Part II, the deduction of depreciation reserve from the gross rate base is proper. There is no merit to Penn Water's claim that under Section 3 (13) its reserve for depreciation can be deducted from its rate base only to the extent, if at all, that its income remaining after deduction of operating expenses including normal depreciation expense has been in excess of a fair return. Since only depreciation charges in the operating section of the income statement are reflected in the reserve for depreciation, Penn Water's contention in effect is that it is not this normal depreciation reserve but only a special kind of a depreciation reserve accumulated out of excessive profits which is to be deducted. Under this construction a licensee could, over the entire period of its license, be entitled to rates sufficient both to recover 100% of its capital investment and to earn a return on the full investment, including the part already recovered by virtue of the deduction of depreciation as an ordinary expense.

By this contention, Penn Water seeks to take advantage of the changed point of view toward

depreciation accounting since the enactment of Section 3 (13) in 1920. While it is customary today to consider depreciation expense as part of operating expenses and to deduct it before computing net return, it was still not unusual in 1920, when the Federal Water Power Act was enacted, to determine profits without deduction for depreciation and to consider normal depreciation as coming out of "profits" instead of constituting a cost of service to be charged to operating expense. See *First Annual Report to Congress*, H. Doc. No. 242, 67th Cong., 2d Sess., p. 58; Hatfield, *Modern Accounting* (1915), pp. 290-291; May, *Twenty-Five Years of Accounting Responsibility* (1936), p. 164; Mason, *Principles of Public-Utility Depreciation* (1937), p. 104. It was in light of this practice of considering depreciation expense as coming out of profits instead of operating expenses that Section 3 (13) referred to the depreciation reserve as accumulated from "earnings in excess of a fair return." The testimony of Mr. O. C. Merrill (an engineer, not an accountant),⁸⁶ who assisted in the preparation of the bill which eventually became the Federal Water Power Act, makes it clear that, notwithstand-

⁸⁶ At the hearings Mr. Merrill represented the Secretaries of War, Agriculture, and Interior, who comprised the Commission under the Act as originally enacted (41 Stat. 1063). Hearings, House Committee on Water Power, 65th Cong., 2d Sess., pp. 4, 5. He afterwards became the Commission's first Executive Secretary. H. Doc. 242, 67th Cong., 2d Sess., pp. 10-11.

ing the language used, (1) Section 3 (13) refers to the usual, not special, depreciation charges, and (2) the provision regarding net investment was intended to assure to licensees the return of 100%, but not more, of its investment. Hearings before the House Committee on Water Power, 65th Cong., 2d Sess., pp. 34-35, 41, 42-43.

In these circumstances, both the Commission's reading of Section 3 (13) to provide for the deduction of depreciation reserve from the rate base to the extent that the company had fully earned a fair return in addition to normal depreciation expense, and its deduction of such amount of depreciation reserve here are clearly sound. There could, therefore, be no conflict in the present case between a Section 3 (13) "net investment" rate base and the rate base used by the Commission in fixing rates under Part II.⁸⁷

⁸⁷ Neither *Alabama Power Co. v. Federal Power Commission*, 128 F. 2d 280, 293 (C. A. D. C.) nor *Niagara Falls Power Co. v. Federal Power Commission*, 137 F. 2d 787 (C. A. 2), certiorari denied, 320 U. S. 792, supports Penn Water's claim of conflict between Parts I and II in regard to rate formulas. Neither case was a rate case, involved Part II, or suggested the possibility of a conflict. Moreover, when the court in the *Alabama* case suggested that different formulas apply to licensees and nonlicensees, it was referring to Section 20 which limits licensees to rates fixed on no more than a net investment rate base, whereas at that time, "fair value" under *Smyth v. Ames*, 169 U. S. 466, was still applicable to nonlicensees. Not only did the court in the *Alabama* case plainly regard the Part I formula as lower, rather than higher, than Part II's (128 F. 2d at 293) but the removal of the "fair value" requirement for nonlicensees by *Federal*

This conclusion that the rate base provisions of Parts I and II were "substantially identical" was reached by the Third Circuit in the *Safe Harbor* case after a thorough consideration of the problem. 179 F. 2d at 187-188, 193-199. Clearly, there is no basis for Penn Water's argument that Part I cannot be applicable to licensees because of a difference in the statutory rate making formulas.

D. IF SECTION 20 AND PART II SHOULD BE DEEMED IN CONFLICT,
THE LATTER SHOULD PREVAIL

Rejection of the foregoing reconciliation of Section 20 and Part II would not mean that because of the potential conflict between these provisions, licensees which qualify as "public utilities" should nevertheless not be regulated as such under Part II. The question then would be how to choose between repeal of Section 20 *pro*

Power Commission v. Hope Natural Gas Co., 320 U. S. 591, wiped out even this difference. And in the *Niagara* case, the court in discussing the rate base under Part I, used "net investment" and legitimate cost interchangeably, with its reference to Section 20 presumably indicating that it was speaking of them in terms of a maximum (137 F. 2d at 792-793). In addition, the court in the *Niagara* case made it clear that it did not regard any differences between Parts I and II as exempting licensees from Part II; the court explicitly recognized that licensees which qualify as "public utilities" are not exempt from regulation under Part II, by speaking of "nonlicensed public utilities" and by referring to Part II as relating "*principally* to rates of public utilities engaged in interstate commerce other than licensees under Part I" (italics supplied) (137 F. 2d at 795).

tanto by implication, unfavored though that be, and an even more extensive nullification of Part II by implied exception, which is no more favored. Even express exceptions from a general policy which a law embodies should be strictly construed. *Interstate Natural Gas Co. v. Federal Power Commission*, 331 U. S. 682, 690-691; *Spokane & Inland R. R. v. United States*, 241 U. S. 344, 348, 350; cf. *Piedmont & Northern Ry. v. Interstate Commerce Commission*, 286 U. S. 299, 311, 312; *United States v. McElvain*, 272 U. S. 633, 639.

Implied repeal of Section 20, *pro tanto*, would require only that to the extent that that Section confers jurisdiction on states to regulate by agreement interstate *wholesale* rates of licensees that are also "public utilities" (which we have shown it doesn't), it shall be deemed repealed by Part II. This is in striking contrast to the breadth of effect the exemption of licensees would have in nullifying a number of important provisions of Part II as far as these licensee-public utilities are concerned. Among the provisions so nullified would be the compulsory interconnection and service provisions of Sections 202 (b) and 207; the war and other emergency compulsory interconnection and service provisions of Section 202 (c); the regulation of sales, leases, dispositions, and mergers of facilities, and acquisition of securities of other public utilities, of Section 203;

the rate schedule filing provisions for suspension of changes in rates of Section 205; the prohibition of "insiders' profits" and payment of dividends out of capital of Section 305 (a); and the regulation of interlocking directors and officers of Section 305 (b). No justification for striking down all these provisions is offered by Penn Water, and it is hardly possible that Congress intended such a result without a word in the statute or in the legislative history manifesting that intention. As the Third Circuit said in the second *Safe Harbor* case (179 F. 2d 179, at p. 186, note 10):

* * * If the provisions of the respective [Parts] cannot be reconciled then [Part I] must be deemed to be repealed by [Part II] * * *

Penn Water contends that Part II may not be applied to it because its license gives it contractual rights which may not be modified by subsequent changes in the statute. See Section 28. Penn Water admits that its license was issued in 1951, long after the enactment of Part II. Nor does it point to any provision of its license which is contravened by Part II. Part I spells out the conditions on which licenses are granted, and the provisions of Part I may thus be deemed to be terms of the license; but we have shown that none of these provisions is in conflict with Part II.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the judgment below be affirmed.

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